TRANSCRIPT OF RECORD

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1934

No. 289

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

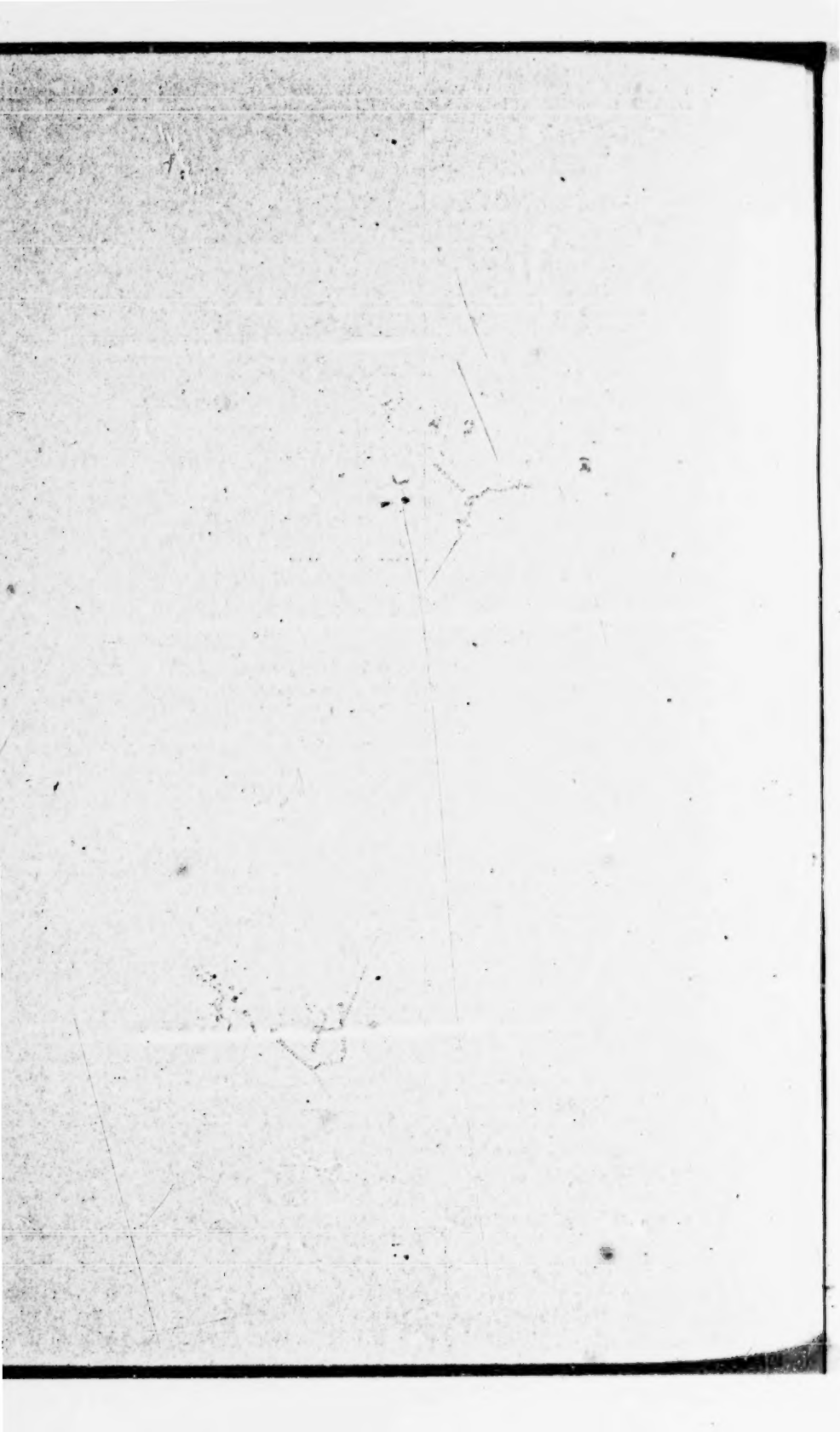
vs.

WALTER W. TAYLOR

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

PETITION FOR CERTIORARI FILED AUGUST 14, 1934

CERTIORARI GRANTED OCTOBER 8, 1934



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1 *Proceedings before United States Board of Tax Appeals*

Docket entries

Docket No. 56876

WALTER W. TAYLOR, PETITIONER

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appearances:

For Petitioner: Wm. P. Jeffery, Esq. (withdrawn); Truman Henson, Esq.
For Respondent: O. W. Swecker, Esq., C. A. Ray, Esq.

1931

Apr. 20—Petition received and filed. Taxpayer notified. (Fee paid.)
" 20—Copy of petition served on general counsel.
May 14—Answer filed by general counsel.
" 25—Copy of answer served on taxpayer—assigned to General alendar.

1932

Aug. 11—Hearing set October 10, 1932.
" 25—Motion to postpone hearing to November 14, 1932, filed by taxpayer. October 29, 1932, granted.
Nov. 14—Hearing had before Mr. Trammell on merits. Submitted. Briefs due in 60 days and 10 days to reply.
" 29—Transcript of hearing of November 14, 1932, filed.

2 1933

Jan. 13—Brief filed by general counsel.
" 13—Brief filed by taxpayer. January 16, 1933, copy served on general counsel.
" 24—Reply brief filed by taxpayer.
Apr. 22—Memorandum opinion rendered, Charles M. Trammell, division 2. Judgment will be entered under rule 50.
May 13—Notice of settlement filed by general counsel.
" 17—Hearing set June 7, 1933, on settlement.
June 7—Hearing had before Mr. Morris, division 14, on settlement under rule 50—not contested—referred to Mr. Trammell for decision.
" 9—Decision entered—C. M. Trammell, division 2.
Aug. 30—Notice of the withdrawal of William P. Jeffery as counsel for taxpayer.
" 30—Notice of the appearance of Truman Henson as counsel for taxpayer.

1933
" 30—Hearing had before Mr. Adams (Trammell) on motion of petitioner for new trial—argued and motion overruled. Respondent's verbal motion to strike affidavits from petitioner's motion for new trial denied but said affidavits received only in support of motion. Motion for new trial filed.
" 30—Motion for new trial filed at hearing—denied.
Sept. 7—Transcript of hearing of August 30, 1933, filed.
3 Sept. 8—Petition for review by United States Circuit Court of Appeals (Second) with assignments of error filed by taxpayer.
" 8—Proof of service filed by taxpayer.
" 29—Agreed statement of evidence lodged.
" 29—Agreed statement of evidence approved and ordered filed.
Oct. 26—Praecipe for record filed—proof of service thereon.
Nov. 6—Order enlarging time for transmission of record to December 1, 1933, entered.

Petition.

Filed April 20, 1931

(Title omitted.)

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency dated February 20, 1931,
4 and accompanying statement initialed IT:AR:A-2 UVT-60 D, and as a basis for his proceeding alleges as follows:

I. Petitioner is an individual residing at Deer Park, Greenwich, Conn., and with a place of business at 111 Broadway, New York, N.Y.

II. The notice of deficiency (a copy of which is attached and marked "Exhibit A") was mailed to petitioner on February 20, 1931.

III. The taxes in controversy are income taxes for the calendar year 1928 and are for approximately $9,156.69.

IV. The determination of tax set forth in said notice of deficiency is based upon the following error:

The Commissioner increased the item of profit on sale of securities from $2,970 theretofore reported by petitioner to $50,228.84.

V. The facts upon which the petitioner relies as the basis of this proceeding are, upon information and belief, as follows:

1. In August, 1927, petitioner acquired all the stock of three public utility corporations, viz: Chester Water and Light Company, Reading Light & Power Co. and Brownsville Electric Co. and all of the net assets of the Chittenden-Pittsford Distribution System. The business last mentioned was thereupon incorporated by petitioner.

2. The petitioner paid for the stocks and property aforesaid and the same cost petitioner $96,030. Such sum represented the fair market value of said stock and property and the same did not have a value, market or otherwise, in excess of said sum.

3. That thereafter petitioner transferred to the Allied Public Service Corporation, a corporation organized under the laws of Delaware, all of the stock of the four utility companies mentioned above and received in exchange therefor shares of the Allied Corporation as follows:

1,000 shares no-par-value preferred stock.
2,500 shares no-par-value class A common stock.
5,000 shares no-par-value class B common stock.

The foregoing represented all of the stock of the Allied Corporation at any time outstanding. The Allied Corporation owned no property other than the utility stocks so acquired.

4. That preferred stock of the Allied Corporation was entitled to $6 cumulative preferred dividends; was preferred as to assets at $100 per share, and was callable at $105 per share. Both the A and B stocks were subordinate to the preferred stock as to dividends and as to assets. The class A stock was callable at $35 per share. The class B stock had full voting power.

5. That between August 1927, when petitioner acquired said stock and properties at a cost of $96,030, and October 1927, when petitioner transferred the same to the said Allied Public Service Corporation, there had been no change in the value of said stocks and properties and no change in business conditions affecting the value thereof, and the same were in October 1927 of a fair market value not exceeding $96,030, the cost thereof to petitioner.

6. That in the spring of 1928 there was a marked and unusual activity in connection with public utility stocks and properties. This was in large measure due to activity on the part of large utility companies to increase and round out their holdings in properties by the acquisition of small independent units. Prior to this change in conditions and the unusual and unprecedented demand for public utility properties, the Allied Corporation had attempted to effect a sale of the properties acquired by it but was unable to interest anyone in the purchase of said properties until about April 1928.

The Allied Company was negotiating with one company for the sale of these properties, and was prepared if necessary to accept the offer of such company of $125,000, when negotiations were opened with another utility company which was enlarging its chain of holdings, and in May 1928 the Allied Corporation sold all of the said properties to the second company for $205,599.94. The price finally secured for such properties was in a large measure due to the competition between the prospective purchasers. The properties sold had a special value to the purchaser—a value beyond their

intrinsic worth and normal market value. The difference between the original cost and the sale price represented an appre-
7 ciation in value which occurred in the spring of 1928.

7. Following the sale of said properties by the Allied Corporation such corporation purchased from petitioner 1,000 shares of the preferred stock theretofore issued to petitioner, and petitioner received therefor the sum of $99,000.

8. During the time such properties were held by the Allied Corporation it expended the sum of $10,669.78 in the maintenance thereof. That the Allied Corporation in its income-tax return for the year 1928 reported and paid a tax on a profit on said sale of $98,900.16, being the sale price less petitioner's cost and the maintenance expense.

9. That petitioner in his income-tax return for the year 1928 allocated his entire cost, $96,030, to the preferred stock of the Allied Corporation acquired by him and allocated no cost to the A and B stocks for the reason that the preferred stock had preference over the A and B stocks of $100,000, and the then total and market value of all of the stocks of the Allied Corporation acquired by the petitioner was only $96,030, all of which lay solely in the preferred stock. No market value was represented by the A and B stocks at the time the same were acquired. That petitioner in his income-tax return reported a profit from the sale of said preferred stock of $2,970, being the difference between original cost, $96,030, and sale price, $99,000.

10. That respondent has refused to accept such allocation
8 and profit as reported by petitioner, and for the purpose of petitioner's 1928 income tax has assigned $48,771.16 as the cost of the preferred stock acquired and sold by petitioner, thus leaving $47,258.84 as the cost of the A and B stocks and has computed the profit to petitioner on the sale of such preferred stock on such basis to wit; cost as determined by respondent, $48,771.16; sale price, $99,000; profit, $50,228.84.

11. The foregoing cost to petitioner for such preferred stock—$48,771.16—was determined by assuming the cost to petitioner of said Allied Corporation preferred stock was 99,000 (proceeds to petitioner) 194,950ths (proceeds to Allied Corporation less maintenance cost) of $96,030 (cost to petitioner).

Wherefore, your petitioner prays that this Board hear the proceeding and determine that petitioner's cost of 1,000 shares of preferred stock of Allied Public Service Corporation was $96,030 and not $48,771.16 as found by respondent and that petitioner's profit on the sale thereof was $2,970 and not $50,228.84 as found by the respondent.

Respectfully submitted.

WILLIAM P. JEFFERY,
Attorney for petitioner.

STATE OF NEW YORK,
County of New York, *ss.*:

Walter W. Taylor, being duly sworn, says that he is the
9 petitioner above named; that he has read the foregoing petition, or had the same read to him, and is familiar with the statements contained therein, and that the facts stated are true, except as to those facts stated to be upon information and belief, and those facts he believes to be true.

WALTER W. TAYLOR.

Subscribed and sworn to before me this 17th day of April 1931.

DENTON MCKANE,
Notary Public.

Kings Co. No. 119, Reg. No. 3002. Cert. filed in N.Y. Co. No. 17, Reg. No. 3–Mc–8. Commission expires March 30, 1933.

Exhibit A to petition

NP–2–28

TREASURY DEPARTMENT.
OFFICE OF COMMISSIONER OF INTERNAL REVENUE,
Washington, Feb. 20, 1931.

MR. WALTER W. TAYLOR,
111 Broadway, New York, New York.

SIR: You are advised that the determination of your tax
10 liability for the year(s) 1928 discloses a deficiency of $9,156.69, as shown in the statement attached.

In accordance with section 272 of the Revenue Act of 1928, notice is hereby given of the deficiency mentioned. Within sixty days (not counting Sunday as the sixtieth day) from the date of the mailing of this letter, you may petition the United States Board of Tax Appeals for a redetermination of your tax liability.

However, if you do not desire to petition, you are requested to execute the enclosed agreement form and forward it to the Commissioner of Internal Revenue, Washington, D.C., for the attention of IT:C:P–7. The signing of this agreement will expedite the closing of your return(s) by permitting an early assessment of any deficiency and preventing the accumulation of interest charges, since the interest period terminates thirty days after filing the enclosed agreement, or on the date assessment is made, whichever is earlier; whereas if no agreement is filed, interest will accumulate to the date of assessment of the deficiency.

Respectfully,

DAVID BURNET,
Commissioner.
By (Signed) J. C. WILMER,
Deputy Commissioner.

Enclosures:
Statement.
Form 882.
Form 870.

11 *Answer*

Filed May 14, 1931

[Title omitted.]

The Commissioner of Internal Revenue, by his attorney, C. M. Charest, General Counsel, Bureau of Internal Revenue, for answer to the petition filed in the above-entitled appeal, admits and denies as follows:

1, 2, and 3. Admits the allegations in paragraphs 1, 2, and 3.

4. Denies the notice of deficiency is based upon the errors alleged and set forth in paragraph 4.

5. (1) Admits the allegations in paragraph 5(1).

5. (2) Admits that stock cost petitioner $96,030.00, but denies all other allegations in paragraph 5(2).

5. (3) Admits that petitioner transferred his stock in the four utility companies to the Allied Public Service Corporation
12 for 1,000 shares of preferred, 2,500 shares of class A common and 5,000 shares of class B common stock of said Allied Public Service Corporation, but denies all other allegations in paragraph 5(3).

5. (4 to 11) Denies the allegations in paragraphs 5(4 to 11).

Wherefore, it is prayed that the taxpayer's appeal be denied.

(Signed) C. M. CHAREST,
General Counsel,
Bureau of Internal Revenue.

Of Counsel:

W. FRANK GIBBS,
Special Attorney, Bureau of Internal Revenue.

Memorandum opinion

Filed April 22, 1933

[Title omitted.]

William P. Jeffery, Esq., for the petitioner.
Owen W. Swecker, Esq., for the respondent.

TRAMMELL: This is a proceeding for the redetermination of
13 a deficiency in income tax for 1928 in the amount of $9,156.69. The error assigned is that the Commissioner erroneously increased the item of profit on sale of securities from $2,970, reported by the petitioner in its return, to $50,228.84.

The petitioner is an individual residing at Deer Park, Greenwich, Connecticut. In August 1927, and for some years prior thereto, the petitioner was employed by the Associated Gas & Electric Company. His duties consisted in seeking out, examining into, and purchasing

public utility properties for that company. He was paid a commission based on the properties purchased. Shortly before August 1927 the petitioner secured options upon either the stocks or properties of four public utilities companies, giving him the right to purchase same as follows:

	Purchase price
Chester Water & Gas Company, located at Chester, Vermont	$36,000
Reading Light & Power Company, located at Reading, Vermont	9,500
Brownsville Electric Light Company, located at Brownsville, Vermont	4,500
Chittenden-Pittsford Distribution System, located at Pittsford, Vermont	45,000

According to the arrangement between petitioner and the Associated Company, the petitioner was required to first offer properties to the Associated Company, and if that company did not buy, petitioner was privileged to offer them elsewhere or to purchase them himself. Petitioner offered the above mentioned properties to the Associated Company. That company refused to purchase them. Thereupon petitioner purchased them himself, paying the amounts above stated. The petitioner purchased all the stock of the corporations except that of the Chittenden-Pittsford Distribution System. Instead of purchasing stock in the latter company, he purchased all of the assets. After purchasing the assets of the Chittenden-Pittsford Distribution System, the petitioner organized a corporation known as the Allied Vermont Corporation, and turned the assets over to that company for capital stock. On October 13, 1927, the petitioner organized the Allied Public Service Corporation, and exchanged the stock of the four above-mentioned companies for all the stock of the new corporation, consisting of 1,000 shares, no par value, preferred stock; 2,500 shares, no par value, common stock, class A; and 5,000 shares no par value, common stock, class B. The preferred stock was entitled to cumulative preferred dividends at the rate of $6 per share and was callable at $105 per share. The class A stock was callable at $35 per share.

In May 1928 the Allied Public Service Corporation sold the stocks of these four utility companies for $194,930.16. Thereafter, in the year 1928, the petitioner sold his preferred stock in the Allied Public Service Corporation to that corporation, receiving therefor $99,000. The petitioner in his income-tax return reported the sale of this preferred stock of the Allied Public Service Corporation and assigned $96,030 as the cost thereof and $99,000 as the sales price thereof, with resulting profit of $2,070.

When the petitioner transferred the stocks of the utility companies to the Allied Public Service Corporation receiving in exchange therefor all the stock of the latter company the transaction came under the reorganization provisions of the Revenue Act of 1926 and resulted in no tax at that time. This being true, the basis for determining gain or loss with respect to the sale of the stock of the Allied Public Service Corporation received by petitioner would be the same as the stock exchanged therefor. The petitioner, how-

ever, did not sell all the stock but only the preferred. The question is what is the basis for determining gain or loss of the preferred stock received by petitioner in the exchange.

In the case of Glenn S. Curtiss et al., 21 B.T.A. 629, we held that when securities of a single class are exchanged for new securities of different classes so that no gain or loss is realized, for the purpose of determining gain or loss on the subsequent sale of any of the new securities the proportion of the original cost or other basis to be allocated to each class of new security is that proportion which the market value of the particular class bears to the market value of all securities received on the date of the exchange. An allocation according to this principle is not questioned in this case.

The respondent fixed the cost of the Allied Public Service Corporation preferred stock sold by the petitioner at $48,771.16 by allocating that much of the total value of all stocks to the preferred stock. This cost was reached by a mathematical formula stated as follows:

$$\frac{\$99,000.00}{\$194,930.17} \times \$96,030 = \$48,771.16.$$

16 This cost, deducted from the admitted sale price, $99,000, produced a profit of $50,228.84.

The respondent determined the value of all the stock received in the exchange was $194,930.17. The petitioner claims that the value of all stock received in the exchange was $96,030, that is that all value should be attributed to the preferred stock. The question, however, is not what was the total value of all the securities received in exchange, but the value of the preferred stock, or rather what proportion of the total value of all securities is to be attributed to the preferred stock. It may well be that the properties acquired or all the classes of stocks received by the petitioner were worth only $96,030 as the petitioner contends and yet the preferred stock which petitioner sold may have had the value of $48,771.16 as determined by the respondent. It is obvious that even if all the securities were worth only $96,030 that the proportionate value of the preferred stock to all the stocks would not necessarily be different from that determined by the Commissioner.

The petitioner would question only one term in the proportion, that is, he contends that the amount of $96,030 should be substituted for $194,930.17 in the formula adopted by the respondent. However, this does not necessarily change the result. The very evidence which tends to show that $194,930.17 is not correct tends equally to show that $99,000 was not the value of the preferred stock when received in the exchange in 1927. If one of the two terms in the pro-

17 portion or formula is incorrect, the other must also be incorrect. If the preferred stock was not worth $99,000 at the time of the exchange and another numerator is to be substituted for that amount is the formula, as well as another amount in the denominator, the quotient may, for all the record discloses, be the same. At least there is no testimony to show that it is incorrect. Cf. Alexander Sprunt & Son, Inc. v. Commissioner, — Fed. (2d) —, decided April 4, 1933.

The testimony does not show that all of the value of all of the securities received in this exchange is to be attributable to the preferred stock. There were two other classes of stock. It may well be, for all the record discloses, that these other stocks had substantial value. There is no testimony as to the earnings or dividends or the reasonable prospects therefor or any other factor which would tend to show that the other classes of stock had no value. It is contended by the petitioner, however, that owing to the preferences attributable to the preferred stock that the common stock had no value unless the preferred stock was worth $100,000. The question, however, is one of fact to be determined by testimony and not theory. It is conceivable that common stocks may actually sell on the market when preferred stocks in the same corporation are selling at less than par. In any event, we do not think that the petitioner has shown that the amount allocated to the preferred stock sold by him is any different from that determined by the Commissioner by testimony which shows that the total value of all classes of stock is different from that used by the respondent in a formula for the purpose
18 of determining the value of the preferred stock. We accordingly approve the determination of the respondent.

Reviewed by the Board.

Judgment will be entered under rule 50.

Enter:

Entered April 22, 1933.

Decision

Entered June 9, 1933

[Title omitted.]

Pursuant to the determination of the Board, as set forth in its memorandum opinion entered April 22, 1933, it is

Ordered and decided: That there is a deficiency in tax of $9,156.69 for 1928.

Enter:

Entered June 9, 1933.

Member.

[SEAL]

19 *Motion for new trial*

Filed August 30, 1933

[Title omitted.]

Comes now, Walter W. Taylor, the petitioner above named, by Truman Henson, his attorney, and moves this honorable Board that it grant a new trial in the above-entitled proceeding to receive evidence as to whether it be practicable to apportion the cost basis to your petitioner of his stock in the Allied Public Service Corporation

between his preferred and common stocks therein, and if the same appear to be practicable, as to what proportion of said cost basis should be allocated to said preferred stock.

The grounds upon which this motion is based are as follows:

First, that this proceeding was tried by both petitioner and respondent upon a theory which the Board, in its opinion, held to be erroneous, in consequence of which evidence sufficient to allow the Board to decide the cause upon its merits was not introduced, for the evidence presented was only that which was relevant to said
20 erroneous theory. And, second, that not only is that state of facts ample ground for granting a new trial, but also where, as here, the respondent's determination is clearly erroneous (as is hereinafter set out), the Board should not, for lack of proof by petitioner, redetermine the clearly erroneous deficiency determined by the respondent, but should receive further evidence to enable it to determine the just result upon the merits.

The only question presented in this proceeding is the cost basis to your petitioner of the preferred stock in the Allied Public Service Corporation received by him together with the common stock of said corporation on or about October 13, 1927. Petitioner, at that time, transferred to said corporation assets which he had acquired in August 1927, at a cost of $96,030.00, and in return therefor received all of the stock of said corporation, consisting of 1,000 shares no-par preferred (entitled to cumulative dividends at $6 per share per annum and to $100 per share upon liquidation), 2,500 shares no-par class A common, and 5,000 shares no-par class B common. In May 1928 said corporation sold its assets for $194,930.16, and thereafter, and during said year, said preferred stock was sold to said corporation by petitioner upon the payment to him of the sum of $99,000.00; and the question presented is the cost basis to petitioner of such preferred stock and the amount of income realized by him upon said sale. The cost basis of said preferred stock, as determined by the respondent, was that proportion of the cost basis of all the stock which said amount of $99,000.00, received by petitioner,
21 as aforesaid, upon the sale of his said preferred stock, bore to $194,930.16, the price received by said corporation upon the sale of its assets in May 1928. During the period from the receipt by the petitioner of the stock of said Allied Public Service Corporation on October 13, 1927, to May 1928, when the assets thereof were sold, a period of seven months, there was, as appears from the testimony of petitioner herein, a large appreciation in the values of public utility stocks.

Whereas it was and is conceded that the cost basis of all the stock must be apportioned between the respective classes on the basis of their respective market values, this case was tried by both petitioner and respondent upon the theory that if the total value of the assets acquired by said corporation did not at the time of such acquisition exceed the sum ($100,000) to which, by reason of its prefer-

ence, the preferred was entitled upon liquidation, then it followed, as a matter of law, that neither class of common had any value and that therefore the total cost to petitioner of the assets exchanged by him for such stock should be allocated in its entirety to the preferred.

As appears from the supporting affidavits of William P. Jeffery, former counsel for petitioner herein, and of Walter R. Bullock, petitioner's accountant, the foregoing theory was agreed to at the trial by counsel for the respondent; and the only questions asked of the witness at the trial by counsel for either party and the only matters treated in either brief, were as to the value of the
22 assets acquired by said corporation at the time the same were acquired, for under the agreed theory of the case that was the only material fact. As aforesaid, said theory was that although the cost of all the stock (or the cost of the assets which were exchanged for all the stock) must be apportioned between the respective classes of stock on the basis of their respective market values, nevertheless if it were shown that the value of the assets exchanged for the stock did not, at the date of the exchange, exceed the amount to which the preferred was entitled on dissolution, then it followed, as a matter of law, that the market value of each class of common was zero and, in consequence, that the cost of all the stock must be apportioned to the preferred. In view of this theory of the case, the only evidence adduced, and the only arguments advanced by either side were with respect to the value of said assets at the time the same were exchanged for the stock.

No contention is made that even a formal written stipulation to this effect would bind the Board. On the contrary, it is freely admitted that parties are not competent to stipulate questions of law. But it is most earnestly urged that where, due to trial on an erroneous theory, particularly when it is the theory adopted by both sides, evidence sufficient to decide a cause on its merits has not been introduced, a new trial should be granted to receive such further evidence as will permit a decision on the facts. "Trial on an erroneous theory would ordinarily be abundant reason for justifying the court in granting a new trial * * *" 46 C. J. 86.

Frink v. Commercial Bank, 195 Iowa, 1011, 1022; 191 N.W. 513, 519.

23 In Underwood v. Commissioner, 56 Fed. (2d) 67, where the case was tried on an erroneous theory and the petitioner having failed to prove his case on a proper theory, the deficiency determined by the respondent was redetermined by the Board, the decision of the Board was reversed and new trial ordered; and the Circuit Court of Appeals said, in part, p. 73:

"* * * there is the well-established rule that an appellate court has the power, without determining and disposing of a case, to remand it to the lower court for further proceedings if the case has been tried on a wrong theory, or the record is not in condition for

the appellate court to decide the question presented with justice to all parties concerned. See Finefrock v. Kenova Mine Car Co. (C.C.A.), 22 F. (2d) 627, 634, and cases cited: also Seufert Bros. Co. v. Lucas (C.C.A.), 44 F. (2d) 528.

"Reversed and remanded."

Dermott v. Wallach, 66 U.S. (1 Black) 96, 98.

"* * * there has been a mistrial below, for which the judgment must be reversed, and the case sent down, and a new venire ordered. There is a good bar to the action remaining untried, and not yet found for the plaintiff. * * *."

Iroquois Furnace Co. v. Wilkin Manufacturing Co., 181 Ill. 582, 600; 54 N.E. 987, 993.

"Where a case is tried upon an erroneous or mistaken theory of law, the judgment should be reversed, and the case sent back for a new trial."

24 Sensfelder v. Stokes, 69 N.J. Law 86, 89; 54 Atl. 517, 518.

"For it is well settled that a verdict cannot be supported upon a theory of law contrary to that upon which the case was submitted to the jury."

Painter v. Hudson Trust Company, 2 N.J. Misc. 1137, 1139; 126 Atl. 636, 637.

"* * * for it is entirely settled that, unless a verdict can be supported upon the theory of the law on which the case was submitted to the jury, it must be set aside."

Napoli v. Erie Railroad Co., 165 N.Y. Sup. 206, 208.

"* * * the issues having been disposed of at the trial upon the theory that the defendant by its deviation was a converter of the property entrusted to its care, which theory the trial court thereafter held to be inapplicable, and defendant being thus deprived of the right to go to the jury on the question whether the damage was caused by the failure of the defendant to follow the direction contained in the bill of lading, there must be a new trial."

Union Pacific Railway Co. v. Springsteen, 41 Kan. 724; 21 Pac. 774, where the court's headnote was, in part, as follows:

"A new trial should be granted when it appears that the only theory upon which a judgment could be sustained is upon a
25 phase of the action not tried, but practically ignored, and another phase thereof appeared to have been thoroughly tried, and regarded by all as the important and pivotal part of the case."

Having no evidence before it upon which it could decide the cause upon its merits, and having determined that the theory upon which the trial was had was erroneous, the Board herein redetermined the deficiency as determined by the respondent. On the evidence in the record, the only fact which the Board could find was the value on October 13, 1927, of the assets on that day transferred to the Allied Public Service Corporation, and this, it was held, was insufficient to form a basis for a decision on the merits; and, as aforesaid, the Board redetermined the respondent's determination for petitioner's failure to prove his case.

Whereas, it is freely admitted that a final determination of the Commissioner of Internal Revenue is, in the ordinary case, presumptively correct and entitled to redetermination by the Board in the absence of proof by the petitioner that it is erroneous and that another determination is correct, the rule is subject to the exception that if the Commissioner's determination is erroneous as a matter of law, it should not be redetermined by the Board, even though the petitioner fail to prove his case, but in such circumstances the Board should receive further evidence to enable it to determine the true and just result and make its redetermination upon the result of such inquiry.

26 In Underwood v. Commissioner, 56 Fed. (2d) 67, 72, the Circuit Court of Appeals for the 4th Circuit said, in part, in its opinion:

"It is settled that the taxpayer has the burden of proof by a number of decisions of the Supreme Court. * * * But we do not think that this rule so restricts the powers of the Board as to require it to countenance an obvious injustice. * * *

"The Board had ample power under the statute to require the production of additional evidence when it became clear that it could not do justice to the taxpayer by reason of the deficiencies in the record before it. It was unquestionably incumbent upon the taxpayer to offer the testimony in the first instance, and cases arise where the moving party must suffer the consequences of his own neglect. Here, however, * * * the Commissioner's action was wrong in a material respect. The information to correct the mistake was readily obtainable * * *. Under these circumstances, the Board should have deferred its decision until testimony showing the amount of the deductions to which the taxpayer was entitled was introduced, and then have redetermined the deficiency. The decision of the Board will therefore be reversed and the case remanded * * *. * * *. In a number of instances, Circuit Courts of Appeals have remanded case for rehearing when it seemed necessary in order to do justice to the parties. It does not appear in these cases that new evidence was available; but in the instant case the

27 evidence is known to exist and it would be an abuse of discretion to decline to receive it. * * *"

Again in Collin v. Commissioner, 32 Fed. (2d) 753, 754, where the question, as here, was the proportion of the cost of a block of preferred and common stock to be allocated to one of the classes of stock, and, the petitioner having failed to make his proof, the plainly erroneous determination of the Commissioner was redetermined, the Circuit Court of Appeals for the Sixth Circuit laid down the rule in these words:

"We are satisfied that some part of the total price paid for the stock units was paid for the common stock—what part we are unable to determine on the record here. Upon another hearing it may be practicable to obtain data or facts upon which a fair apportionment of cost as between the two classes of stock may be made, but, if it

should not be, then under article 39 of Regulation 45, the petitioner will not be chargeable with any profits until he shall have recovered the entire purchase price."

In Russell v. Commissioner, 45 Fed. (2d) 109, 103, the Circuit Court of Appeals for the First Circuit said, in part:

"While there is a presumption that the Commissioner's findings are correct, * * * when it appears, as in this record it does appear, that the methods pursued by the Commissioner were
28 mathematically and legally erroneous, that presumption no longer avails."

And in Cohan v. Commissioner, 39 Fed. (2d) 540, the Circuit Court of Appeals for the Second Circuit reversed and remanded a decision of the Board redetermining, for lack of proof by the petitioner, a deficiency determined by the Commissioner, but clearly erroneous.

In our case the petitioner did not, at the trial had herein, offer evidence as to the market values of the respective classes of stock received by him on October 13, 1927, when he acquired all of the stock of the Allied Public Service Corporation, and on that ground the Board redetermined the deficiency determined by the respondent in his notice of deficiency. The respondent's determination, however, was clearly erroneous and it is submitted that a new trial should be had to receive further evidence and determine whether it be practicable to allocate a part of the cost of all of the stock to the preferred, and, if so, what part should be so allocated.

That the respondent's apportionment, as contained in his said determination, is erroneous, is clear. He has applied against the cost of all the stock a fraction, the denominator of which is the amount received by the corporation as the price of its assets seven months after the petitioner's acquisition of the stock, and the numerator of which is the amount received by petitioner upon the sale of his preferred stock. It is petitioner's contention that however correct respondent's ratio of the values of the different classes of
29 stock may have been as of the date of the sale of the assets of the corporation in May 1928, it is erroneous on its face, as a matter of law, to assert that the same ratio was applicable as of a date 7 months earlier when the total value of the corporation's assets was about half what it was in May 1928. As a matter of law, the ratio of the values of preferred and common stock at one date is no evidence whatever of the ratio of the values thereof at a different date.

Kirkland v. Commissioner, 57 Fed. (2d) 608.

While it is true that the value of an asset on one date may be some evidence of its value on another date, it does not follow that the ratio between preferred and common stock on one date is evidence of the ratio at a different time. It is too much to assume that two different classes of stock, one preferred, and one common, appreciate or depreciate at the same rate. On the contrary, common

experience would lead to the opposite conclusion; and this is particularly true in a situation such as that presented in the instant case where the total value of the assets of the corporation is approximately equal to the retirement value of the preferred stock on one date, and approximately twice that amount on the other date. In view of the testimony in the record that the assets of the corporation were worth about $96,030.00 in October 1927 (the retirement value of the preferred being $100,000), that there was a rapid rise in the public utilities market between October 1927 and May 1928, and that said assets were sold in May 1928 for $194,930.16, it would appear that the ratio between the preferred and common as
30 of May 1928 must of necessity be different from that of October 1927. The Court of Appeals of the District of Columbia took judicial notice in the Kirkland case of the fact that common and preferred stocks appreciate at different rates and we submit that it is even plainer here that this common must have appreciated to a greater extent than the perferred. In point of fact, in these circumstances, the ratio of May 1928 is evidence only of what was not the ratio of October 1927. The May 1928 ratio is not evidence of the October 1927 ratio and to use it as such is error as a matter of law.

In the Kirkland case, supra, the question, as here, was the ratio between preferred and common stock. The two classes of stock were purchased in a block in 1923. In 1924 there were actual ascertainable market values for each class but the ratio of values could not be determined as of the time of the purchase by then existing evidence. As in our case, the Commissioner determined that ratio by means of the ratio of the later date, and petitioner not offering any proof as to the respective values of the classes of stock at the time of purchase, the Board redetermined the deficiency in accordance with the Commissioner's determination. On appeal to the Court of Appeals of the District of Columbia, however, this was reversed and the court said in part, at page 610:

"* * * it is not known whether this relation remained constant: that is to say, whether the advance in value of preferred and common was in the same ratio as the stocks bore to each
31 other at purchase: indeed, the probabilities are otherwise. Without this, it follows that it is impracticable, even under the method adopted by the Commissioner, to apportion the original cost * * *, and it was just to meet a condition such as this that article 39 of Regulations 65 was adopted."

It is submitted that not only under the authority of the Kirkland case, but also as is clearly apparent from the facts and circumstances herein, the respondent's determination is plainly erroneous as a matter of law; and that, because of such error, and upon the authority of the above cited decisions of four different Circuit Courts of Appeal and the Court of Appeals of the District of Columbia, the presumption of the correctness of respondent's determination is rebutted, or does not apply.

From the annexed affidavits in support of this motion, it appears that none of the stock of the Allied Public Service Corporation was listed or dealt in on any exchange at or about October 13, 1927, that there were no sales thereof at or about that date; and that the anticipated earnings of the corporation were not sufficient to pay any dividends on either class of the common stock. If a new trial is granted as herein prayed, petitioner will offer evidence indicative of whether it be practicable to apportion the cost basis of all the stock between the preferred and common, and if so, in what proportion.

Wherefore, your petitioner moves this honorable board that it grant a new trial herein to receive evidence as to whether it
32 be practicable to determine what part of the cost basis of all of said stock should be apportioned to the preferred, and if it appear to be practicable so to do, then to determine the part of such total cost so allocable to the preferred.

An oral hearing on this motion is requested.

Dated the 29th day of August, 1933.

(Signed) TRUMAN HENSON
TRUMAN HENSON,
Counsel for Petitioner,
Office and P.O. Address, 26 Liberty Street, New York City.

Affidavit of Walter R. Bullock

STATE of NEW YORK,
County of New York, ss.:

Walter R. Bullock, being duly sworn, deposes and says:

1. I am a certified public accountant, with office at 31 Nassau Street, city, county and State of New York, and I am familiar with the accounts and records of the Allied Public Service Corporation.

2. I have examined the data accumulated for Mr. Walter W. Taylor during the year 1927, upon the basis of which Mr. Taylor decided to purchase the stock or assets of Chittenden-Pittsford Distribution System, Chester Water & Light Company, Reading Light & Power Company, and Brownsville Light & Power Company, and from my examination of said data I am able to state,
33 upon information and belief, that said data discloses that the combined net income of said four companies for the year 1926, which was the last full year of operation of said companies prior to the formation of said Allied Public Service Corporation, was the sum of $9,536.54; and that said total combined net income in said sum of $9,536.54 was before any deduction for depreciation, Federal income taxes, or any costs for engineering management fees or holding company overhead expenses.

3. From my said examination of said data I am also able to state, upon information and belief, that the same contain appraisals of the reproduction value, after allowance for observed depreciation, of

the assets of said four companies, and that the same disclose a total value of depreciable assets as of the summer of 1927 in the sum of $84,620, which, at a composite depreciation rate of 5% would make an annual depreciation deduction of $4,231.00, thus reducing the aforesaid combined net income of said four companies to $5,305.54 before Federal income taxes and costs for engineering management fees and holding company overhead expenses.

(S.) WALTER R. BULLOCK.

[*Duly sworn to by Walter R. Bullock; jurat omitted in printing.*]

34 *Affidavit of Walter R. Bullock*

STATE OF NEW YORK,
County of New York, ss.:

Walter R. Bullock, being duly sworn, deposes and says:

1. I am a certified public accountant, with office at 31 Nassau Street, city, county, and State of New York, and I was associated with Mr. William P. Jeffery in the trial of Walter W. Taylor v. Commissioner, Docket No. 56876.

2. I was present at said trial and during the course of said trial Mr. Jeffery stated that he understood that the respondent agreed that if it be established that the market value of all of the assets of the Allied Public Service Corporation on October 13, 1927, when said assets were acquired by said corporation, was not in excess of $96,030.00, then the cost basis to Mr. Taylor of said preferred stock was $96,030, and that in that event all of the cost of all of the stock in the Allied Public Service Corporation should be allocated to the preferred; and Mr. Swecker indicated his assent to this statement either in words or by nodding his head, or by some other indication of assent. I do not find this assent to be expressed in the record herein, but the same was expressed at the trial as aforesaid.

(S.) WALTER R. BULLOCK.

[*Duly sworn to by Walter R. Bullock; jurat omitted in printing.*]

35 *Affidavit of William P. Jeffery*

[Title omitted.]

STATE OF NEW YORK,
County of New York, ss.:

William P. Jeffery, being duly sworn, deposes and says, that he is the attorney for the petitioner in the trial of this proceeding before the Board of Tax Appeals.

Considerable discussion between trial counsel and the Board member is not set forth in the minutes of the proceedings. In the course of the discussion deponent, as counsel for petitioner, stated in effect

that as he understood the situation the sole issue was the value in October 1927 of certain properties acquired by Mr. Taylor in August 1927 and transferred by him to the Allied Corporation in October of that year; that if the value of these properties in October was the amount paid therefor by Mr. Taylor in August, then the assessment was improper and should be set aside, but that if the value of said properties was the sale price thereof in the following May, then the assessment was proper and should be sustained.

In the course of the discussion following the presentation of
36 this point, counsel for the Commissioner concurred in the proposition outlined above. At one point in the discussion the Board member inquired of counsel for the Commissioner if he concurred in the statement as to the issue and the effect of value determination as of October 1927. Counsel for the Commissioner stated that he concurred. While the record does not show all this discussion, the correctness of the foregoing statements is apparent from the record, and direct support for same is contained in the briefs submitted by counsel for the Commissioner.

WILLIAM P. JEFFERY.

[*Duly sworn to by William P. Jeffery; jurat omitted in printing.*]

Affidavit of Walter W. Taylor

STATE of MICHIGAN,
County of Berrien, ss.:

Walter W. Taylor, being duly sworn, deposes and says:

1. I am the petitioner above named, and I was president and
37 treasurer of the Allied Public Service Corporation from its formation in the year 1927 and throughout the year 1928.

2. There were no sales of any of the stock of said corporation at or about the time of the issuance of said stock to me nor at any other time; and none of said stock was listed, or dealt in, on any exchange at or about said time of the issuance of said stock to me, nor any time.

(S) WALTER W. TAYLOR.

[*Duly sworn to by Walter W. Taylor; jurat omitted in printing.*]

Substitution for counsel and notice of appearance

Filed August 30, 1933

[Title omitted.]

In accordance with rule 36, William P. Jeffery, of #1
38 Wall Street, city, county, and State of New York, hereby withdraws as counsel for the petitioner in the above-entitled proceeding; and Truman Henson, of #26 Liberty Street, city,

county, and State of New York, whose mailing address is #26 Liberty Street, New York City, hereby appears as counsel for said petitioner in the above-entitled proceeding.

WILLIAM P. JEFFERY.
TRUMAN HENSON.

Dated New York, N.Y., August 29, 1933.

———— ————,
Petitioner.

Petition for review

Filed September 8, 1933

[Title omitted.]

To the Honorable the Judges of the United States Circuit Court of Appeals for the Second Circuit:

Comes now, Walter W. Taylor, the petitioner in the above-
39 entitled proceeding, and petitions for review by the United States Circuit Court of Appeals for the Second Circuit, of the decision of the United States Board of Tax Appeals entered herein on June 9, 1933, redetermining the deficiency, in the sum of $9,156.69, in your petitioner's Federal income tax for the calendar year 1928, theretofore determined by the respondent in his deficiency notice; and of the decision of the United States Board of Tax Appeals denying your petitioner's motion for a new trial; and respectfully shows, upon information and belief, as follows:

I

Your petitioner, Walter W. Taylor, is an inhabitant of the town of Greenwich, county of Fairfield and State of Connecticut, within the second circuit.

II

STATEMENT OF THE CONTROVERSY

The only question involved herein is whether it be practicable fairly to apportion between preferred and common, as of the date of acquisition, the total cost to your petitioner of certain preferred and common stock acquired by him for a lump sum; and if it be practicable so to apportion such cost, then what proportion thereof should be allocated to the preferred, all of which was sold by your petitioner in the year 1928.

On or before October 13, 1927, petitioner transferred, in
40 a nontaxable exchange, certain assets which had cost him $96,030.00 to the Allied Public Service Corporation and received in return therefor all of its capital stock, to wit, 1,000 shares no

par value preferred stock entitled to cumulative dividends at the rate of $6.00 per share per annum, and to $100.00 per share on liquidation; 2,500 shares, class A no par value common stock; and 5,000 shares, class B no par value common stock. During the period from October 1927 to May 1928 there was a rapid appreciation in the public utilities market. At or about the middle of May 1928 said Allied Public Service Corporation sold its assets for the sum of $194,930.16, and thereafter petitioner sold all of his preferred stock in said Allied Public Service Corporation to said corporation and received therefor the sum of $99,000.00. The question presented is, as aforesaid, the cost basis to your petitioner of said 1,000 shares of preferred stock.

The respondent, in his notice of deficiency, determined the cost basis of said preferred stock to be that proportion of the cost of all the stock which the sum received by petitioner upon the sale of said preferred stock, or $99,000.00, bore to the sum which said corporation received for its assets, or $194,930.16.

From such deficiency notice, petitioner took his appeal to the United States Board of Tax Appeals and thereafter a trial was had and briefs were filed by petitioner and respondent.

At said trial an agreement was entered into between counsel for petitioner and counsel for respondent to the effect that if it appeared

41 that the value of the assets acquired by the Allied Public Service Corporation from the petitioner in exchange for all of its stock was, at the time said assets were so acquired by said corporation, not in excess of the amount to which said preferred stock would have been entitled upon a liquidation, to wit, $100,000.00, then it followed that the preferred stock was the only stock of the Allied Public Service Corporation having any value; that the value of each class of common stock was zero; and that a fair apportionment of the cost of all of the stock would be to allocate all of said cost, or $96,030.00, to the preferred stock alone.

In consequence of said agreement, said trial was conducted upon such agreed theory; and petitioner introduced no evidence except such as was relevant to said theory, to wit, evidence relative to the value of the assets acquired by said Allied Public Service Corporation at the time the same were so acquired by it.

Thereafter, the Board of Tax Appeals rendered its opinion, holding that whether or not the value of the assets acquired by said Allied Public Service Corporation was, at the time the same were acquired, only $96,030.00, nevertheless it did not follow that the preferred was the only stock which had any value; and further holding that the petitioner, having introduced only such evidence as was relevant to said agreed theory, had not introduced evidence upon which the proceeding could be decided upon its merits; and further holding that the determination made by the respondent, from which petitioner had appealed to the Board, was entitled to a presumption of correctness and should be redetermined.

42 Thereafter, and on June 9, 1933, the Board entered its decision redetermining said determination made by the respondent in his notice of deficiency.

Thereafter, your petitioner moved said Board that it grant a new trial herein for the purpose of receiving evidence as to whether it be practicable fairly to apportion the cost basis of all of said stock, between the preferred and the common stock, and if it appear to be so practicable, as to what proportion of said cost should be so apportioned to the preferred. Annexed to said motion and in support thereof, petitioner filed affidavits setting out the fact of said agreement of counsel as to the aforesaid theory upon which the case was tried, and also further affidavits disclosing that there is in fact evidence upon which the Board of Tax Appeals could find whether said fair apportionment was practicable and if so what said apportionment should be. Said affidavits further set forth that such evidence is that there had been no sales of the stock of the Allied Public Service Corporation at or about the time the same was received by the petitioner; that said stock had never been listed or dealt in on any exchange, and that the anticipated profits of said Allied Service Corporation were not sufficient to pay any dividend upon any of said stock, except the preferred; and petitioner offered in said motion that if a new trial were granted he would produce evidence indicative of whether such fair apportionment were practicable, and if so, what the same should be.

In his said motion, petitioner urged that where a case has been tried by all parties upon an erroneous theory and the only
43 evidence submitted is such as is relevant to such erroneous theory alone, a party should not be penalized for failing to introduce other evidence at the trial, but that the Board should grant another trial or hearing and receive evidence upon which the case may be decided upon its merits. Petitioner further urged in said motion that in any event, and whether or not he should have been penalized for not introducing such further evidence at the trial, the respondent's said determination was so wrong as to be arbitrary, groundless, and fanciful; and that in view of such arbitrary, groundless, and fanciful nature of respondent's said determination, the same was not entitled to the presumption of correctness to which respondent's determinations are ordinarily entitled and should not have been so redetermined by the Board, but that the Board should inquire as to the facts to an extent sufficient to allow it to do justice to the parties. The ground upon which petitioner asserted respondent's said determination to be arbitrary, groundless, and fanciful was that for the purpose of determining the ratio between the preferred and common stocks as of the date of acquisition thereof by petitioner, respondent used, not a ration of the market values of the stocks as of that date, but a ratio as of a date seven months later, whereas, as a matter of law, in circumstances where, as here, there has been a very large appreciation amounting

to approximately 100% in the value of the assets of the corporation, and where, before such appreciation, the value of said assets was approximately equal to the liquidation value of the preferred stock,

a ratio between the classes of stock as of a date after the
44 appreciation has taken place, is no evidence of what the ratio between the classes of stock was before the appreciation, but, on the contrary, can be evidence only of what that ratio was not at the date before the appreciation took place.

After hearing said motion for new trial, the Board of Tax Appeals denied the same, and your petitioner brings this petition for review.

III

DESIGNATION OF COURT OF REVIEW

Your petitioner, being aggrieved by said decisions of the United States Board of Tax Appeals, and being an inhabitant of the town of Greenwich, county of Fairfield and State of Connecticut, which is within the Second Circuit, petitions for a review by the United States Circuit Court of Appeals for the Second Circuit of said decisions of the United States Board of Tax Appeals.

IV

ASSIGNMENT OF ERRORS

Your petitioner, as a basis for review, assigns the following errors committed by the United States Board of Tax Appeals herein:

(1) The Board erred in failing to find that the determination of the respondent from which petitioner appealed to the Board herein was erroneous as a matter of law.

(2) The Board erred in finding that the cost basis to your
45 petitioner of his preferred stock in said Allied Public Service Corporation was $48,771.16, for said finding was unsupported by any evidence, or by any presumption.

(3) The Board erred in making any decision of the case upon the evidence received.

(4) The Board erred in failing to require or admit further evidence.

(5) The Board erred in redetermining a deficiency in your petitioner's 1928 income tax in the sum of $9,156.69.

(6) The Board erred in failing to find that there was no deficiency in your petitioner's income tax for 1928.

(7) The Board erred in denying petitioner's motion for new trial.

Wherefore your petitioner prays that this honorable court may review said decisions of the United States Board of Tax Appeals and reverse and set the same aside, and that the clerk of the United States Board of Tax Appeals be directed to transmit and deliver to the clerk of this honorable court certified copies of all and every

documents and records necessary and material to the presentation and consideration of the foregoing petition for review and as required by the rules of this honorable court and the statutes made and provided; and that this court review the decisions of the United States Board of Tax Appeals herein and direct the entry of a
46 decision by said Board that there is no deficiency in petitioner's said income taxes for the calendar year 1928; and your petitioner further prays for such other and further relief as may seem to this honorable court to be just and in the premises warranted.

(Signed) TRUMAN HENSON.
TRUMAN HENSON,
Attorney for Petitioner,
Office and P.O. Address, 26 Liberty Street, New York City.

Duly sworn to by Walter W. Taylor; jurat omitted in printing.

47 *Notice of filing petition for review*

(Filed Sept. 8, 1933.)

[Title omitted.]

To E. BARRETT PRETTYMAN, Esq.,
General Counsel,
Bureau of Internal Revenue, Washington, D.C.,
Attorney for the Respondent.

SIR: Please take notice that on the 8th day of September 1933 the undersigned presented to this Board and filed with the clerk thereof the petition of Walter W. Taylor, a copy of which is annexed hereto, for the review, by the United States Circuit Court of Appeals for the Second Circuit, of the decisions of the Board in the above-entitled proceeding.

Dated Washington, D.C., September 8, 1933.

(Signed) TRUMAN HENSON,
Attorney for the Petitioner,
26 Liberty Street, New York City.

48 Service of the within notice and copy of petition for review is admitted this 8th day of September 1933.

(Signed) E. BARRETT PRETTYMAN.

Statement of the evidence

(Filed Sept. 29, 1933.)

[Title omitted.]

The above-entitled cause came on for hearing before the Honorable Charles M. Trammell, member of the United States Board of Tax Appeals, in Washington, D.C., on the 14th day of November 1932,

there being present the petitioner by his then counsel, William P. Jeffery, and the respondent by his counsel, Owen W. Swecker (C. M. Charest, then general counsel, Bureau of Internal Revenue).

The petitioner, to maintain the issues on his behalf, intro-
49 duced the oral testimony of Walter W. Taylor and various documents marked Petitioner's Exhibits 1, 2, 3, and 10, respectively, which were duly admitted in evidence. The Board of Tax Appeals made no separate findings of fact herein, but found that the cost basis to petitioner of his preferred stock in the Allied Public Service Corporation was $48,771.16, which was the cost basis thereof determined by respondent in his notice of deficiency. In the petition for review of the Board's decision, error has been assigned that said finding was unsupported by any evidence; that the respondent's said determination was plainly wrong and not entitled to the presumption of correctness accorded it by the Board; that the Board should have made no decision of the case upon the evidence received, but should have granted petitioner's motion for new trial and received the further evidence offered by petitioner.

Walter W. Taylor, having been called as a witness on behalf of petitioner and having been duly sworn, testified upon direct examination in substance as follows:

Petitioner was, in 1928, in the business of public utility broker, employed by the Associated Gas & Electric Company, and his duties were buying electrical public utility properties of the same type as those involved in this proceeding. It was a part of his duties to investigate properties, ascertain whether they could be purchased and, if so, whether they could be purchased on terms satisfactory to said Associated Gas & Electric Company; and to carry through the purchases if said company so desired. He had been en-
50 gaged in such business for some years and was compensated therefor by a salary and commissions.

In the year 1927, petitioner, in the course of his said employment, investigated four disconnected properties, consisting of four electrical distribution systems located in different parts of the State of Vermont; and entered into negotiations for the purchase thereof. Said properties were by name: Chester Water & Light Company, Reading Light & Power Company, Brownsville Electric Company and Chittenden-Pittsford Distribution System. Petitioner offered said properties to said Associated Gas & Electric Company, but said company declined to purchase the same and petitioner thereupon, and as he was entitled under the terms of his employment to do, purchased the same himself in August 1927 at a total cost of $96,030. Petitioner had had no prior connection with any of said properties and the transaction was one where the vendors sought to get as much as they could and petitioner sought to get the properties as reasonably as possible. Petitioner supplemented his own judgment of the values of said properties by employing a firm of electrical engineers, whom he considered qualified, to make an in-

vestigation; and said engineers made such investigation and rendered a report on such values to petitioner.

In purchasing said properties, petitioner purchased all of the stock of the respective corporations owning three of the same and purchased the assets of the fourth; and petitioner thereupon caused a corporation to be formed to which he transferred the assets of said fourth property, receiving all of the stock of said corporation in return. Upon the acquisition of said stocks and
51 assets, petitioner also caused another corporation known as the Allied Public Service Corporation, to be formed to take over all of said properties, and the certificate of incorporation thereof was filed on September 1, 1927. Shortly thereafter, and on October 13, 1927, petitioner transferred to said Allied Public Service Corpofation all of the capital stock of said three corporations which he had purchased and also the stock of the corporation he had formed to take over the assets of the fourth of said properties, and petitioner received in return therefor all of the stock of said Allied Public Service Corporation. The capital stock of said Allied Public Service Corporation consisted of 1,000 shares of no-par value preferred entitled to cumulative dividends of $6 per share per annum and to $100 per share on liquidation before any distribution to any other stock, and callable at $105 per share; 2,500 shares class A, common, entitled to $35 per share on liquidation before any distribution to the class B stock; and 5,000 shares class B, common, which was entitled on liquidation to any balance after the payment of $100 per share to the preferred and $35 per share to the class A stock. A certificate of stock of said Allied Public Service Corporation, setting out the rights of such classes of stock in substance, as aforesaid, was offered and received in evidence and marked Petitioner's Exhibit No. 1.

The witness, continuing under direct examination, further testified in substance as follows:

After said transfer, petitioner owned all of the stock of said Allied Public Service Corporation, and said Allied Public Service Corporation owned all of the stock of said four public utility
52 companies; and said Allied Public Service Corporation thereafter operated said four companies.

Thereafter, and in the late winter of 1927, or the early spring of 1928, petitioner started negotiations on behalf of said Allied Public Service Corporation for the sale of the stocks of said four public utility companies, and in the course of said negotiations, came into contact with the Colonial Utilities Corporation. Petitioner finally entered into an agreement with said Colonial Utilities Corporation on behalf of said Allied Public Service Corporation, and said Allied Public Service Corporation sold the stocks of said four utility companies to said Colonial Utilities Corporation for $194,930.16 in cash.

Thereafter, and during the year 1928, petitioner sold to said Allied Public Service Corporation said 1,000 shares of said preferred stock

of said Allied Public Service Corporation for $99,000 cash; and on his income-tax return for said year 1928, petitioner reported said sale price of $99,000, and a cost of said 1,000 shares of preferred stock of $96,030, and a profit on the transaction of $2,070.

Under date of November 13, 1930, petitioner received a letter from the Treasury Department, which letter was offered and received in evidence, and marked Petitioner's Exhibit No. 2, to show how the respondent arrived at his computation of profit. In said letter one-third of said $96,030 was assigned to said preferred stock as the cost basis thereof, one-third of said $96,030 was assigned to said class A common stock, and one-third to said class B common stock.

53 Under date of February 5, 1931, petitioner received a further letter from the Treasury Department which assigned a different cost basis to said 1,000 shares preferred stock of said Allied Public Service Corporation. Said Treasury Department letter dated February 5, 1931, was offered and received in evidence, and marked Petitioner's Exhibit No. 3, for the purpose of showing the basis of respondent's determination as set out in his notice of deficiency herein and respondent's computation of petitioner's profit on said sale of said 1,000 shares of preferred stock. Said letter disclosed respondent's said determination to be that the cost basis to petitioner of said 1,000 shares of preferred stock was $48,771.16 and that petitioner's profit on said transaction was $50,228.84. Said cost basis of $48,771.16 for said preferred stock was computed by respondent by applying against $96,030 the cost basis of all of petitioner's stock in said Allied Public Service Corporation a fraction, the denominator of which was $194,930.16, the sum for which said Allied Public Service Corporation sold the stocks of said four public utility companies in May 1928 and the numerator of which was $99,000, the sum received by petitioner upon the sale of said 1,000 shares of Allied Public Service Corporation stock thereafter.

The witness, continuing under said direct examination, further testified in substance as follows:

Prior to either conducting or closing negotiations with the Colonial Utilities Corporation, petitioner interviewed other companies to see whether or not they would be interested in purchasing said public utility properties but did not come to any agreement with

54 them. Among others, petitioner interviewed the New England Public Service Corporation and in the course of his negotiations, petitioner received a letter from said New England Public Service Corporation. The properties for the sale of which petitioner was negotiating were the same properties which petitioner had acquired and transferred to the Allied Public Service Corporation.

The Colonial Utilities Corporation approached petitioner and asked if he knew of some small properties located in New England which they could acquire for approximately $200,000. It seemed that they needed about that much property to enable them to finance properties which they already had and make a public bond issue.

They wanted the properties to be in New England because the balance of their properties were located in that vicinity and because the name of their company was the Colonial Utilities Corporation. Petitioner told them that he had four such properties himself which he would sell them for approximately that figure. They seemed to be interested and sent their engineers to make an investigation and came back to petitioner and entered into negotiations, at the end of which the transaction was closed. During the period from the purchase of said four public utility companies by petitioner until the Allied Public Service Corporation sold the same, there had been certain additions put into the properties, some current assets, some quick assets, some working capital, and some profit accrued, so that there were, when the Allied Public Service Corporation sold said properties, additional assets in the total amount of about $10,000.

55 At the time petitioner purchased said properties, he personally investigated the same and examined into their earning statements and records.

The Colonial Utilities Corporation was a new company which had been organized, under which there had been gathered together a group of previously independent companies. The securities of the companies so acquired by the Colonial Utilities Corporation were not on the public market and the Colonial Utilities Corporation bought its said subsidiaries for the purpose of putting out securities to sell through banks, and explained to petitioner that they needed to get about $200,000 more in their balance sheet in order to build their company to a size to make it marketable from a banking standpoint. Before that conversation, petitioner had not made the Colonial Utilities Corporation an offer, at which the Allied Public Service Corporation would sell, but that conversation suggested to petitioner the price to ask from the Colonial Utilities Corporation. Petitioner had previously sought to secure offers from other companies and had been unable to secure any offers from other companies for such figures or anywhere near such figures, nor had he been able to secure any definite offers, although he had tried to do so.

Between August and October 1927, or the date when petitioner acquired said four public utility properties and the date when the same were transferred to the Allied Public Service Corporation, nothing of consequence occurred in the utility market, but thereafter, and beginning in January 1928, and continuing to some time beyond May 1928, there was a considerable difference in the utility field, the acquisition or desire to acquire subsidiaries by larger utility groups and a boom in the utility field.

56 The Colonial Utilities Corporation was not an Insull subsidiary but the New England Public Service Company was.

A map of the State of Vermont with red circles thereon was shown to the witness and the witness identified said red circles as representing the locations of said four public utility properties at Pittsford, Vt., Chester, Vt., Brownsville, Vt., and Reading, Vt. Such

map was offered and received in evidence, and marked "Petitioner's Exhibit No. 10."

Continuing under direct examination, the witness further testified as follows:

Reading and Brownsville, for which properties petitioner paid $9,500 and $4,500, were fairly close together. Chester was approximately twenty miles from Reading or Brownsville. Chester was from forty to fifty miles from Pittsford. Pittsford was thirty to forty, or forty-five to fifty, miles from Reading. Except for Brownsville and Reading, said properties were not contiguous and did not serve adjoining or touching territory. There were other companies in between, serving the districts between the two larger of said companies, both as between themselves and as between them and the small companies.

Beginning in the early part of 1928, there was great activity among the large holding companies for the acquisition of smaller properties. This became more pronounced in the early part of 1928 than prior thereto. Petitioner was familiar with what was going on in the utilities field, both from the standpoint of market prices publicly and the action of the various companies in assembling group
57 properties. The public was demanding public utility securities; they were paying higher and higher prices, and it was much easier for the holding companies to finance the purchase of properties by reason of the fact that they could dispose of their securities to the public at a very high price, which enabled them to do financing at a very low rate and they could afford to pay high prices. Due to the popularity of such properties, and the fact of a lower yield than theretofore being acceptable to the public, the utilities companies, in assembling properties for the purpose of public offerings, could pay more and did pay more. It was a demand which became very pronounced in the early part of 1928 which permited that form of operation and financing.

The direct examination of the witness concluded at this point.

Upon cross-examination, petitioner testified in substance as follows:

In August 1927 he purchased the entire capital stock of the Chester Water and Light Company and the Reading Light & Power Company and the Brownsville Electric Company, and the assets of the Chittenden-Pittsford Distribution System. The assets of Chittenden-Pittsford Distribution System were subsequently incorporated and known as the Allied Vermont Company and the entire capital stock thereof was transferred to petitioner. Petitioner then turned over to the Allied Public Service Corporation the stocks of said four corporations and in return received 1,000 shares no-par value preferred stock; 2,500 shares no par value common class A; and 5,000 shares no par value common class B. The class A
58 stock had no voting rights, the class B common had voting rights, and the preferred stock had no voting rights except in case of default.

After petitioner acquired said four public utility companies in August 1927, he operated the same from his office in New York until they were transferred to the Allied Public Service Corporation. The same people carried on the operation in the territories under petitioner's supervision and the supervision of petitioner's engineers. Subsequent to the time that the Allied Public Service Corporation took said four properties over, they were still operated from petitioner's office in New York, but the actual technical operation was handled from the office of Ives and Davidson, petitioner's said engineers, and the financial operations were handled from petitioner's office in New York. The operations went on just the same. The engineers began their operations simultaneously with petitioner's acquisition of the properties.

Petitioner assumed that the reason the Associated Gas & Electric Company did not want to buy the properties when he offered them to it was that said Associated Gas & Electric Company was not interested in those properties.

Petitioner was not sure of the exact amount by which the assets of said four public utility companies were increased during the period they were operated by him and the Allied Public Service Corporation, but he thought the amount was between five and ten thousand dollars. Said additions consisted of working capital, stock of supplies, one or two small extensions, additions to property, additional meters, additional extensions and lines.

59 The Colonial Utilities Corporation paid the Allied Public Service Corporation for the stocks of said four companies, when they were purchased in 1928, $191,000 and some odd. At that time, the engineers of the Colonial Utilities Corporation made an examination of the properties.

The great increase in the activities of public service stocks began in the late fall of 1927 and continued straight through to May, or into May. Petitioner did not go farther than May in his investigation but there was a great appreciation in values between the late fall of 1927 and May of 1928. Petitioner had been engaged in buying properties for the Associated Gas & Electric Company since 1924 and during the years prior to 1928 and from 1924, petitioner had acquired approximately 30 to 40 properties.

The reason petitioner was able to sell these properties was that the Colonial Utilities Corporation needed an exact amount of assets which was approximately the same amount of assets represented by these particular properties. If petitioner had not had assets equal to the amount which the Colonial Utilities Corporation needed for their particular purpose, probably he would not have sold the whole four as easily as he did. Ordinarily, it would be easier to sell a consolidated group of four properties than to dispose of one single company, but a purchaser might not necessarily be interested in all the properties which one might hold, and in some cases it might be much easier to sell one property than four, depending upon whether the property in which the prospective purchaser was in-

terested was contiguous to such prospective purchaser's own
60 property. It is absolutely not true that in this case, where petitioner had four properties within a radius of 40 or 50 miles that those four properties would control the light and power business of that immediate locality, because a very large holding company, the Insull property, was in and around that vicinity. Said four public utility companies were little distribution systems which purchased their electricity from the large trunk lines, the holding company of which Insull was the head, and most of the bulk of the business was in between and could not be reached at all. Petitioner would have thought that for purposes of purchase by the Insull interests, these four properties would have been more valuable, but the letter received from the New England Public Service Company advised him to the contrary. The New England Public Service Company was the company which theoretically should have operated the property at lower costs than anyone else.

Petitioner attended to drawing up the charter of the Allied Public Service Corporation, and he had the power to state as to whether the preferred stock was callable or whether the class A was callable at a certain figure or whether the class B would be callable at a certain figure.

In petitioner's opinion, consolidation of said four companies did not enhance the value of the stock. The enhancement of the value was due to circumstances, if a buyer wanted properties located in a particular territory, plus the general appreciation of all utility properties during that period; and that was the real reason why
61 petitioner was able to sell these properties at a profit for the Allied Public Service Corporation. Petitioner thought it would have been very hard to dispose of only one of these properties; it depended upon the purchaser. Had the Insull organization, which surrounded the properties at that time, been a willing purchaser, it would have been just exactly as easy to sell one as four, but, to the average purchaser, it probably was easier to sell four in a group; it was in this particular case under petitioner's circumstances. In petitioner's opinion, the value of $194,000 that was received for these properties was based entirely upon the consolidation of them and the further fact that the Colonial Utilities Corporation wanted properties of about that amount.

The cross-examination of the witness concluded at this point.

On redirect examination the witness testified, in substance, as follows:

In his previous experience, petitioner had bought many single companies. There was no connection whatsoever between the said four public utility companies. From the standpoint of operation, they produced no more income when owned by one than as four separate companies. The Insull interests might have been just as interested, or more so, in buying one property than four. Petitioner could not say whether any other person would be more interested in buying the four properties than in buying one. Petitioner, as an

experienced man operating in this field, was unable to state whether four separate unconnected and unrelated companies, from the
62 standpoint of location, are, in the aggregate, more valuable than the sum of four units separately owned. Under certain circumstances, a man or company interested in getting as many companies as he can buy at a given price, would be interested in taking four, and another man or company who might be interested in acquiring a lesser number or amount, would be interested in one. It turns on the particular situation and the desires of particular purchasers.

Petitioner was shown a memorandum which refreshed his recollection, and continuing under redirect examination he testified in substance as follows:

The amount which was included in the four companies when their stocks were sold by the Allied Public Service Corporation but which was not included when said four companies were purchased by petitioner was $10,669.78. Otherwise the properties were the same.

The redirect examination of the witness concluded at this point.

On recross examination petitioner testified, in substance, as follows:

There were no distributions or dividends declared by said four public utility corporations during the period from August to May 1928.

The recross examination of the witness concluded at this point.

On redirect examination petitioner testified, in substance, as follows:

During the time of petitioner's ownership, said four public
63 utility corporations were earning on a basis of between nine and ten thousand dollars a year. No evidence was adduced as to whether said earnings were gross or net, or whether the same were sufficient to make any earnings available for the declaration of dividends by said Allied Public Service Corporation.

Counsel for both petitioner and respondent thereupon stated that they had no further questions and the witness was excused.

Petitioner called no further witnesses and respondent called no witnesses.

The foregoing is the substance of all the evidence adduced at the trial in said proceeding.

(Signed) TRUMAN HENSON.
TRUMAN HENSON,
Attorney for Petitioner,
Office and P. O. Address, #26 Liberty Street, New York City.

Agreed to:
E. BARRETT PRETTYMAN,
General Counsel,
Bureau of Internal Revenue,
Attorney for Respondent.

The foregoing contains the substance of all the evidence given on the hearing of this proceeding and in order that the same may be preserved and made of record, this statement of evidence is duly

stated, approved, signed and ordered to be made of record in the above-entitled cause, this 29th day of September, 1933.

By the Board:

(Signed) CHARLES M. TRAMMELL,
Member.

64 *Praecipe*

Filed October 26, 1933

[Title omitted:]

To the clerk of the United States Board of Tax Appeals:

You will please prepare and, within sixty days from the filing of the Petition for Review, transmit to the clerk of the United States Circuit Court of Appeals for the Second Circuit certified copies of the following documents and records in the above-entitled case:

1. The docket entries of proceedings before the United States Board of Tax Appeals.
2. Pleadings before the Board.
(a) Petition, including annexed copy of notice of deficiency.
(b) Answer.
3. Memorandum opinion of the Board.
4. The decision of the Board entered June 6, 1933.
5. Substitution of counsel and notice of appearance, filed August 30, 1933.

65 6. Motion for new trial, including supporting affidavits as follows: Affidavit of Walter W. Taylor, sworn to September 2, 1933; affidavit of William P. Jeffery, sworn to August 29, 1933; and two affidavits of Walter R. Bullock, sworn to August 28, 1933.

7. Order of the Board denying motion for new trial.
8. Petition for review.
9. Notice of filing petition for review.
10. Statement of evidence.
11. This praecipe.

The foregoing to be prepared, certified, and transmitted as required by law and the rules of the United States Circuit Court of Appeals for the Second Circuit.

Dated New York City, October 23, 1933.

(Signed) TRUMAN HENSON,
TRUMAN HENSON,
Counsel for Petitioner,
Office and P.O Address, 26 Liberty Street, New York City.

Service of a copy of the within praecipe is hereby admitted this 26th day of October, 1933.

E. BARRETT PRETTYMAN,
General Counsel,
Bureau of Internal Revenue.

66 [Clerk's certificate to foregoing transcript omitted in printing.]

67 In United States Circuit Court of Appeals for the Second Circuit

Opinion

Entered May 7, 1934

No. 283. October term, 1933

Argued April 2, 1934. Decided May 7, 1934

WALTER W. TAYLOR, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appeal from the Board of Tax Appeals

Before MANTON, L. HAND, and CHASE, Circuit Judges.

Appeal by a taxpayer from an order of the Board of Tax Appeals fixing a deficiency in his income taxes for 1928.

Trumen Henson, of New York City, for appellant.

Walter L. Barlow, of Washington, D.C., for appellee.

L. HAND, *Circuit Judge:*

This appeal (petition to review) is from an order of the Board of Tax Appeals fixing a deficiency in the taxpayer's income tax for 1928, under the following circumstances: In October 1927 he bought the shares of three small lighting companies in Vermont, and all the assets of a fourth. For all four he paid $96,000, and he at once organized a separate company, to which in consideration of all its shares, he conveyed the assets of the fourth company. Thus armed with the shares of four operating utility companies, he organized a holding company which, in exchange for his shares, issued to him its entire share capital; that is to say: 1,000 shares of preferred stock, without par value, but entitled to $100 on any distribution, callable at 105, and bearing a cumulative dividend of 6%; 2,500 shares of non-par class A stock, redeemable at thirty-five dollars; 5,000 shares of non-par class B stock. In May 1928 another holding company which was on the look-out for job lots of utility shares with which to fill out some projected issues, bought from the taxpayer's holding company all the shares of the four operating companies for $195,000. He thereupon retired the full issue of preferred shares for $99,000, leaving $96,000 in the company's treasury, and having all the class A and class B shares and $99,000 in his own hands. The question is what is the right "basis" of the preferred shares for calculating taxable gain. The Commissioner found this by dividing the original aggregate cost of the properties, $96,000, in the same proportion that the amount at which the preferred shares were redeemed, $99,000, bore to the price paid for all the

assets of the holding company, $195,000. This resulted roughly in allocating $49,000 as "basis" and $47,000 as gain. This the Board affirmed and the case comes here on the taxpayer's appeal.

The Revenue Act of 1928, like its predecessors, gave no clue to the proper treatment of such a problem. The general sections (secs. 111–113 [26 U.S.C.A. §§ 2111–2113]) did not even suggest a solution, and from 1918 forward the Commissioner promulgated a series of regulations to cover it, which have been substantially the same. Article 39, Regulations 45, Revenue Act 1918; article 39, Regulations 62, Revenue Act 1921; article 39, Regulations 68, Revenue Act 1924; article 39, Regulations 69, Revenue Act 1926; article 58, Regulations 74, Revenue Act 1928. That issued under the Revenue Act of 1928 appears in the margin.[1] The meaning of the word "bonus" as there used is obscure. Obviously it does not mean that the actual value of the bonds or preferred shares must exhaust the whole purchase price; if it did there could never be any apportionment. Possibly it is the par of the prior securities, but it is not clear whether the rate of interest or dividends should not come into the computation. For example, suppose that preferred shares with a par of $100 carry a non-cumulative dividend of only four per cent. However well secured they might be they would not sell at par in most markets. Should such shares be estimated at par in determining whether the common shares are a "bonus", or should they be taken at their value, if issued by a company of the most impeccable solvency? These questions we leave unanswered because both sides assume that the common shares at par were a "bonus", as almost certainly they were, whether their par be taken, or the value of a perfectly secure issue of like kind. There was little possibility that in 1927 a preferred share, carrying cumulative 6% dividends, and callable at $105, in an absolutely sound company, would not have been worth $96.

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The preferred shares of the taxpayer's holding company were by no means in that class, and we agree with the Board in thinking that the common shares probably had a value. What that value was we have no means of knowing; the question is whether the taxpayer has shown that at least it was less than the Commissioner's allocation. In deciding the contrary the Board invoked the burden of proof, a rubric which has saved the Treasury many a doubtful case, but which can easily be pushed to deny taxpayers privileges plainly theirs. Here it seems to us a complete non-sequitur to suppose that because in May 1928 the preferred shares were worth about one-half of a total of $195,000 they were worth only that proportion of $96,000 in October of 1927. The preferred shares were a first call

[1] ART. 58. Sale of stock and rights.—* * * Where common stock is received as a bonus with the purchase of preferred stock or bonds, the total purchase price shall be fairly apportioned between such common stock and the securities purchased for the purpose of determining the portion of the cost attributable to each class of stock or securities, but if that should be impracticable in any case, no profit on any subsequent sale of any part of the stock or securities will be realized until out of the proceeds of sales shall have been recovered the total cost.

upon any income up to $6,000; they could not be redeemed for less than $105,000, nor could the common shares get anything in distribution until $100,000 had been paid on them. That such an issue was worth only $49,000 out of $96,000, leaving $47,000 for the common shares, is to our minds too unreasonable to require positive disproof. And when it is attempted to justify such a conclusion affirmatively by the fact that eight months later that was the proportion between the two issues in an aggregate value of nearly twice as much, its arbitrary nature becomes even more apparent. Kirkland v. Burnet, 61 App. D. C. 88, 57 F.(2d) 608.

Nevertheless, while we think that the finding of the Commissioner was wrong, it does not follow that any allocation of the original consideration was "impracticable." True, the shares had just been issued and had therefore never paid a dividend; but the subsidiaries may have had a substantial history and their incomes been reasonably predictable; indeed the evidence was that while the taxpayer owned them, they had a joint income at the yearly rate of $9,000 or $10,000, though whether this was gross or net did not appear. At any rate we cannot say that it was impossible to ascertain the income of the holding company, or with that as datum to estimate the values of the preferred and common shares in October 1927. The taxpayer made no effort to prove that apportionment was "impracticable", excusing himself by exceedingly vague and unsatisfactory affidavits of the existence of an oral stipulation which the Commissioner does not admit to have been made, and which we may not consider. If the burden of proof goes so far as to demand not only that the taxpayer show that the deficiency assessed against him is wrong, but what is the proper deficiency, or that there should be none at all, the decision was right, even though we know that the tax is too high. In an action to recover taxes unlawfully collected the burden does go so far. United States v. Anderson, 269 U.S. 422, 443, 46 S.Ct. 131, 70 L.Ed. 347; Reinecke v. Spalding, 280 U.S. 227, 233, 50 S.Ct. 96, 74 L.Ed. 385. But the reason for this is obvious; a plaintiff, seeking an affirmative judgment measured in dollars, must prove how much is due. His claim is for money paid and he must show that every
69 dollar he recovers is unjustly withheld. So it is not enough merely to prove that the tax as a whole was unlawful; some of the dollars he paid may nevertheless have been due. But this reasoning does not apply when the proceeding is to review an assessment. Although that does indeed partake of the nature of a judgment, and the taxpayer has the burden of proving that it was wrong, after he has done so, he need not, at least under ordinary principles of procedure, prove that he owed no tax, or what was the tax that he did owe. The original assessment rested upon a finding, presumptively correct, but the presumption of its correctness does not extend to other findings which the Commissioner has never made. Any other result would invert the ordinary rules of procedure by imposing a burden of establishing a negative upon

the obligor; indeed of disproving the existence of all possible obligations. It must be owned, however, that the cases are not all in accord, though we do not think that Burnet v. Houston, 283 U.S. 223, 227, 51 S.Ct. 413, 75 L.Ed. 991, should be counted among those which impose such a burden; the facts were quite otherwise. Usually it has been a deduction, not an item of gross income, that has been in question. Saxman C. & C. Co. v. Com'r, 43 F.(2d) 556 (C.C.A. 3); Atlantic Bank & Trust Co. v. Com'r, 59 F.(2d) 363 (C.C.A. 4); Lightsey v. Com'r, 63 F.(2d) 254 (C.C.A. 4). And conceivably as to deductions the rule should be the same as in an accounting where the debtor has the burden of proving all credits. If that be the explanation, this is not such a case, because there is no taxable "gain" until both the receipt and the "basis" are found. But if it be not the explanation, at least the law is not settled, because several Circuit Courts of Appeal have refused to push the burden so far. Having once decided that the finding of the Commissioner was positively wrong they have sent the cause back for a new hearing, although the taxpayer had not proved enough to allow them finally to dispose of the case. Collin v. Com'r, 32 F.(2d) 753, 754 (C.C.A. 6); Rhode Island Hospital Trust Co. v. Com'r, 29 F.(2d) 339 (C.C.A. 1); Strother v. Com'r, 55 F.(2d) 626, 632, 633 (C.C.A. 4); Underwood v. Com'r, 56 F.(2d) 67, 72, 73 (C.C.A. 4); Eau Claire, etc., Co. v. Com'r, 65 F.(2d) 125 (C.C.A. 7); Ferguson v. Com'r, 59 F.(2d) 893 (C.C.A. 10). The statute itself (Revenue Act 1926, § 1003) provides for a rehearing if "justice may require" (section 1226 (b), title 26, U.S. Code, 26 U.S.C.A. § 1226 (b)). It is impossible to suppose that "justice" requires one only in case the Commissioner has failed to make out his case.

Order reversed; cause remanded for further proceedings in conformity with the foregoing.

Chase, Circuit Judge, dissents without opinion.

70 United States Circuit Court of Appeals, Second Circuit

Judgment

Entered May 18, 1934

At a stated term of the United States Circuit Court of Appeals, in and for the Second Circuit, held at the court rooms in the post-office building in the city of New York, on the 14th day of May, one thousand nine hundred and thirty-four.

Present: Hon. MARTIN T. MANTON, Hon. LEARNED HAND, Hon. HARRIE B. CHASE, Circuit Judges.

WALTER W. TAYLOR, PETITIONER

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

Appeal from the United States Board of Tax Appeals

This cause came on to be heard on the transcript of record from the United States Board of Tax Appeals, and was argued by counsel.

On consideration whereof, it is now hereby ordered, adjudged, and decreed that the order of said United States Board of Tax Appeals be, and it hereby is, reversed and cause remanded for further proceedings in conformity with the opinion of this court.

It is further ordered that a mandate issue to the said Board in accordance with this decree.

WM. PARKIN, *Clerk.*

(Endorsed:) United States Circuit Court of Appeals, second circuit. Walter W. Taylor vs. Commissioner of Internal Revenue. Order for mandate. United States Circuit Court of Appeals. Filed May 18, 1934. William Parkin, clerk, second circuit.

71 [Clerk's certificate to foregoing transcript omitted in printing.]

C Supreme Court of the United States

Order allowing certiorari

Filed October 8, 1934

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Second Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

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In the Supreme Court of the United States

OCTOBER TERM, 1934

No. 289

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, petitioner

v.

WALTER W. TAYLOR

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

The Solicitor General on behalf of Guy T. Helvering, Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the Second Circuit entered in the above cause on May 18, 1934, reversing the decision of the Board of Tax Appeals and remanding the cause for further proceedings in conformity with the opinion.

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 12) is unreported. The opinion of the Circuit Court of Appeals (R. 33) is reported in 70 F. (2d) 619.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on May 18, 1934 (R. 36). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the Circuit Court of Appeals erred in remanding this case to the Board of Tax Appeals for a new hearing on the ground that the Commissioner's determination of the amount of income was incorrect, although the taxpayer had failed to prove facts from which a correct determination could be made.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set out in the Appendix, *infra*, pp. 11–13.

STATEMENT

The facts as found by the Board of Tax Appeals (R. 13–16) may be summarized as follows:

Shortly before August 1927 the taxpayer secured options to purchase for specified amounts either the stocks or properties of four public utility companies in Vermont (R. 13). Thereafter, he exercised the options, purchasing the stocks of three of the companies and the assets of the fourth. He then organized a separate corporation to which he conveyed the assets of the fourth company, re-

ceiving its stock in exchange. On October 13, 1927, he organized a holding company to which he conveyed the stocks of the four operating companies and received in exchange all the stock of the holding company, being 1,000 shares of preferred stock without par value, entitled to cumulative dividends of $6 per share and callable at $105 per share; 2,500 shares of Class A no par common, callable at $35 per share; and 5,000 shares of Class B no par common. (R. 14.)

In May 1928 the holding company sold the stocks of these four operating companies for $194,930.16. Thereafter, in the year 1928, the taxpayer sold his preferred stock in the holding company to that company for $99,000. In his income tax return the taxpayer reported the sale of this preferred stock, assigning $96,030, the original aggregate cost of the properties, as the cost of the preferred stock, and $99,000 as the sales price, with resulting profit of $2,970. (R. 14.) When the taxpayer transferred the stocks of the utility companies to the holding company, receiving in exchange therefor all the stock of the latter company, the transaction came under the reorganization provisions of the Revenue Act of 1926, and resulted in no tax at that time. Therefore, the basis for determining gain or loss with respect to the sale of stock of the holding company would be the same as the stock exchanged therefor. The taxpayer, however, did not sell all the stock but only the pre-

ferred, making it necessary to ascertain the basis for determining gain on sale of the preferred stock. (R. 14–15.)

The Commissioner determined the cost to the taxpayer of the holding company's preferred stock to be $\frac{99,000}{194,930.17}$ of $96,030 or $48,771.16, the balance of the $96,030 representing the cost of the common stock (R. 15). This cost, deducted from the admitted sale price, $99,000, produced a profit of $50,228.84 (R. 16).

Upon appeal to the Board of Tax Appeals, the Commissioner's determination was sustained (R. 18).

The Circuit Court of Appeals reversed the decision of the Board of Tax Appeals and remanded the cause to the Board for a new hearing on the ground that the Commissioner's determination of cost basis was wrong, although the taxpayer had failed to introduce evidence to show the correct basis.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that the taxpayer had discharged the burden of proof resting upon him merely by showing that the Commissioner's determination was wrong without proof of facts from which a correct determination could be made.

2. In remanding the cause to the Board of Tax Appeals for further proceedings in conformity with the opinion of the Circuit Court of Appeals.

3. In holding that the Commissioner's determination was plainly erroneous.

4. In reversing the order of the Board of Tax Appeals sustaining the Commissioner's determination.

REASONS FOR GRANTING THE WRIT

1. The instant case, in holding that the taxpayer was only required to show that the Commissioner's determination of cost basis for the preferred stock was incorrect, conflicts in principle with the cases which have established the rule that the burden is on the taxpayer to show the correct amount of the tax in order to have the Commissioner's determination set aside. *Williams* v. *Commissioner*, 45 F. (2d) 61 (C.C.A. 5th); *Becker* v. *United States*, 21 F. (2d) 1003 (C.C.A. 5th); *Saxman Coal & Coke Co.* v. *Commissioner*, 43 F. (2d) 556 (C.C.A. 3d); *Alexander Sprunt & Son* v. *Commissioner*, 64 F. (2d) 424 (C.C.A. 4th); *Atlantic Bank & Trust Co.* v. *Commissioner*, 59 F. (2d) 363 (C.C.A. 4th); *Lightsey* v. *Commissioner*, 63 F. (2d) 254 (C.C.A. 4th); *Matern* v. *Commissioner*, 61 F. (2d) 663 (C.C.A. 9th). The court below, while regarding certain of these cases as distinguishable, conceded that "the cases are not all in accord" and that "at least the law is not settled." 70 F. (2d) 619, 621.

The dissenting judge wrote no opinion, but it seems probable that his dissent was based upon the

foregoing rule, which he had announced in an earlier case, *Darcy* v. *Commissioner*, 66 F. (2d) 581, 585 (C.C.A. 2d), certiorari denied, 290 U.S. 705, as follows:

> The burden is upon the petitioners to show the correct amount of the tax in order to show that the commissioner's determination was wrong. Compare *Burnet* v. *Houston*, 283 U.S. 223, 228, 51 S.Ct. 413, 75 L. Ed. 991; *Reinecke* v. *Spalding*, 280 U.S. 227, 232, 233, 50 S.Ct. 96, 74 L. Ed. 385. * * *

2. The opinion below draws a distinction between suits to recover taxes paid and proceedings to review assessments; also between cases involving deductions and cases relating to income items. The court held that the taxpayer does not have the burden of proving the correct amount of tax when the purpose of the suit is to review assessments of income items, as in the present case. We submit that such a refinement of the rule relating to the burden of proof is unwarranted and that no distinction should be drawn between deductions and income, or between suits for refund and proceedings before the Board of Tax Appeals. It is believed that in all cases the burden is on the taxpayer to show the proper amount of tax. This seems to follow from the proposition that from the beginning the taxpayer is required to show the correct amount of tax and the facts upon which the tax is based. See Sections 51 (a) and 54 (a) of the Revenue Act of 1928, *infra*, p. 11. This burden must per-

sist when the matter of his tax liability is presented to the Board of Tax Appeals for review. Moreover, the fact that a deficiency determined by the Commissioner is too great does not mean that the whole is erroneous; and the taxpayer should be required to show in a proceeding before the Board how much of the deficiency is not due or that no deficiency is owing, for the same reason as in a suit for refund he must show that he is not liable for the whole or a part of the amount collected. In *Becker* v. *United States, supra,* a suit was brought by the United States to recover the amount of an assessment which the taxpayer claimed to be erroneous. The court held that the taxpayer must show how much should be disallowed, since, upon proof that the assessment should be reduced by any particular amount, the Government would still be entitled to recover the remainder.

3. If, as we contend, the principle that the taxpayer bears the burden of proof applies to the instant case, then the Board properly affirmed the Commissioner's determination on the ground that the taxpayer had not proved that the amount to be allocated to the preferred stock was any different from that determined by the Commissioner, and consequently there was no error of law in the Board's decision. Compare *Burnet* v. *Houston,* 283 U.S. 223. The Circuit Courts of Appeals have no power to remand a case unless the decision of the Board is not in accordance with law. Revenue

Act of 1926, Section 1003 (b), *infra*, p. 11. It has been so held in *Houston* v. *Commissioner*, 53 F. (2d) 445 (C.C.A. 3d) and *Thom* v. *Burnet*, 55 F. (2d) 1039 (App. D.C.); and the decision of the Circuit Court of Appeals in remanding the instant case to the Board for a new hearing is in conflict with those cases. But see *Underwood* v. *Commissioner*, 56 F. (2d) 67 (C.C.A. 4th), and authorities there cited.

4. We submit that the court below erred in holding that the Commissioner's determination of the allocated cost of the holding company's preferred stock was plainly erroneous. That conclusion appears to have been based upon the ground that his determination necessarily assumed that the preferred stock was worth only some $49,000 out of a total value of approximately $96,000 for the preferred and common stocks together. Such is not the case. The $48,771.16 assigned by the Commissioner to the preferred stock did not represent its value at date of acquisition by the taxpayer or at any other date, but only the proportionate part of the original cost to the taxpayer of the operating companies which should be allocated to the holding company's preferred stock. Even if the amounts used by the Commissioner in making the allocation, based upon conditions some eight months after the date for valuation, were remote in time, his result nevertheless may have been correct. The basic cost of $96,030 comprised the aggregate price of the original properties as fixed in the options granted

prior to August 1927 (R. 13). The holding company to which the properties were transferred was not organized and the preferred stock was not issued until October 13, 1927, at least two or three months after the date of the options. It is difficult to believe that the preferred and common shares issued by the holding company in connection with the reorganization were not worth more than $96,030 at date of issuance. Certainly such a merger in the fall of 1927 of four small utility companies, with resultant economies of operation and other advantages of combination, would tend to create a total value for the shares of the new company far higher than the sum of the values of the stocks or properties of the four original companies prior to the merger. It would accordingly follow that the value of the preferred and common shares of the holding company at date of issuance was substantially in excess of $96,030. At least, there is nothing to compel the conclusion that they were worth no more.

5. The effect of the decision below is to impose upon the Commissioner the duty of proving a new proposed assessment—a difficult proposition, since the facts with respect to the valuation of assets and the income of the operating companies, which the court suggested as a datum to arrive at the correct basis of the preferred stock, are peculiarly within the knowledge of the taxpayer and his associates. Conceivably, as a result of the court's decision, the Commissioner might have to make a series of

subsequent determinations if the taxpayer shows that each one is wrong without showing the correct amount—clearly an undesirable situation from the standpoint of efficient tax administration. The question thus presented by this case is important not only for that reason but also because the decision of the court below is likely to produce uncertainty and confusion with respect to the proper procedure in cases remanded to the Board.

Wherefore it is respectfully submitted that this petition should be granted.

J. CRAWFORD BIGGS,
Solicitor General.

AUGUST 1934.

APPENDIX

Revenue Act of 1926, c. 27, 44 Stat. 9:

> SEC. 1003. (a) The Circuit Courts of Appeals and the Court of Appeals of the District of Columbia shall have exclusive jurisdiction to review the decisions of the Board (except as provided in section 239 of the Judicial Code, as amended); and the judgment of any such court shall be final, except that it shall be subject to review by the Supreme Court of the United States upon certiorari, in the manner provided in Section 240 of the Judicial Code, as amended.
>
> (b) Upon such review, such courts shall have power to affirm or, if the decision of the Board is not in accordance with law, to modify or to reverse the decision of the Board, with or without remanding the case for a rehearing, as justice may require.
>
> (U.S.C. App., Title 26, Sec. 1226.)

Revenue Act of 1928, c. 852, 45 Stat. 791, 807, 808, 815, 818:

> SEC. 51. INDIVIDUAL RETURNS.
>
> (a) *Requirement.*—The following individuals shall each make under oath a return stating specifically the items of his gross income and the deductions and credits allowed under this title—
>
> * * * * *
>
> SEC. 54. RECORDS AND SPECIAL RETURNS.—(a) *By taxpayer.*—Every person liable to

any tax imposed by this title or for the collection thereof, shall keep such records, render under oath such statements, make such returns, and comply with such rules and regulations, as the Commissioner, with the approval of the Secretary, may from time to time prescribe.

* * * * *

SEC. 111. DETERMINATION OF AMOUNT OF GAIN OR LOSS.—(a) *Computation of gain or loss.*—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the basis provided in section 113, and the loss shall be the excess of such basis over the amount realized.

* * * * *

(d) *Recognition of gain or loss.*—In the case of a sale or exchange, the extent to which the gain or loss determined under this section shall be recognized for the purposes of this title, shall be determined under the provisions of section 112.

* * * * *

SEC. 113. BASIS FOR DETERMINING GAIN OR LOSS.—(a) *Property acquired after February 28, 1913.*—The basis for determining the gain or loss from the sale or other disposition of property acquired after February 28, 1913, shall be the cost of such property; except that—

* * * * *

(6) *Tax-Free Exchanges Generally.*—If the property was acquired upon an exchange described in section 112 (b) to (e), inclusive, the basis shall be the same as in the case of the property exchanged, decreased in the amount of any money received by the tax-

payer and increased in the amount of gain or decreased in the amount of loss to the taxpayer that was recognized upon such exchange under the law applicable to the year in which the exchange was made. * * *

Treasury Regulations 74:

ART. 58. *Sale of stock and rights.*—* * * Where common stock is received as a bonus with the purchase of preferred stock or bonds, the total purchase price shall be fairly apportioned between such common stock and the securities purchased for the purpose of determining the portion of the cost attributable to each class of stock or securities, but if that should be impracticable in any case, no profit on any subsequent sale of any part of the stock or securities will be realized until out of the proceeds of sales shall have been recovered the total cost.

* * * * *

U. S. GOVERNMENT PRINTING OFFICE: 1934

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In the Supreme Court of the United States

OCTOBER TERM, 1934

No. 289

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, petitioner

v.

WALTER W. TAYLOR

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE PETITIONER

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 6) has not yet been reported. The opinion of the Circuit Court of Appeals (R. 33) is reported in 70 F. (2d) 619.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered May 18, 1934. (R. 36.) The petition for a writ of certiorari was filed August 14, 1934, and granted October 8, 1934. The jurisdiction of

this Court is conferred by Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the Circuit Court of Appeals erred in remanding this case to the Board of Tax Appeals for a new hearing on the ground that the Commissioner's determination of the amount of income was incorrect, although the taxpayer had failed to prove facts from which a correct determination could be made.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set out in the Appendix, *infra*, pp. 28–30.

STATEMENT

The pertinent facts may be thus summarized:

Shortly before August, 1927, the taxpayer secured options to purchase for specified amounts either the stocks or properties of four small public utility companies in Vermont. (R. 7.) In August, 1927, he exercised the options, purchasing the stocks of three of the companies and the assets of the fourth and paying therefor $96,030. (R. 3, 7.) He then organized a separate corporation to which he conveyed the assets of the fourth company, receiving its stock in exchange. (R. 7.) On September 1, 1927, he organized a holding company (R. 25) to which, on October 13, 1927, he conveyed the stocks of the four operating companies and received in

exchange all the stock of the holding company, being 1,000 shares of preferred stock without par value, entitled to cumulative preferred dividends of $6 per share and callable at $105 per share; 2,500 shares of Class A no par common, callable at $35 per share; and 5,000 shares of Class B no par common. (R. 7.) The Class B stock had full voting power. (R. 3.) The preferred stock was entitled to $100 per share on liquidation prior to distribution to the other two classes of stock; the Class A common stock was entitled to a preference in distribution of $35 a share over the Class B common. (R. 25.)

In May, 1928, the holding company sold the stocks of these four operating companies for $194,930.16. Thereafter, in the year 1928, the taxpayer sold his preferred stock in the holding company to that company for $99,000. In his income tax return for 1928 the taxpayer reported the sale of this preferred stock assigning $96,030, the original aggregate cost of the stocks and assets acquired by him in August, 1927, as the cost of the preferred stock, and $99,000 as the sales price, with resulting profit of $2,070. (R. 7.) When the taxpayer transferred the stocks of the utility companies to the holding company, the transaction came under the reorganization provisions of the Revenue Act of 1926, and resulted in no tax at that time. Therefore, the basis for determining gain or loss with respect to the sale of the stock of the holding company would be

the same as the stock exchanged therefor. The taxpayer, however, did not sell all his stock in the holding company but only the preferred, making it necessary to ascertain the cost of the preferred stock as the basis for determining the gain on its sale. (R. 7–8.)

The Commissioner determined that of the total cost of $96,030 to the taxpayer for the several classes of stock of the holding company, $\frac{99,000}{194,930.17}$, or $48,771.16, should be allocated to the preferred stock as its cost and the balance to the common stock as its cost. The cost thus apportioned to the preferred stock deducted from the admitted sale price of $99,000 produced a profit of $50,228.84 on the sale of that stock. (R. 8.)

Upon appeal to the Board of Tax Appeals, the Commissioner's determination was sustained on the ground that the taxpayer had not shown that such determination was incorrect, or, in any event, that the amount properly to be allocated to the preferred stock as its cost was any different from that determined by the Commissioner. (R. 9.)

The Circuit Court of Appeals, one judge dissenting, reversed the decision of the Board of Tax Appeals and remanded the cause to the Board for a new hearing on the ground that the Commissioner's determination of cost basis of the preferred stock was wrong, although the taxpayer had failed to introduce evidence to show the correct basis. (R. 33–36.)

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that the taxpayer had discharged the burden of proof resting upon him merely by showing that the Commissioner's determination was wrong without proof of facts from which a correct determination could be made.

2. In remanding the cause to the Board of Tax Appeals for further proceedings in conformity with the opinion of the Circuit Court of Appeals.

3. In holding that the Commissioner's determination was plainly erroneous.

4. In reversing the order of the Board of Tax Appeals sustaining the Commissioner's determination.

SUMMARY OF ARGUMENT

1. The Board of Tax Appeals approved the Commissioner's allocation to the preferred stock of a part of the total cost to the taxpayer of the preferred and common stocks on the ground that the taxpayer had not only failed to show that the Commissioner's allocation was incorrect, but that in any event the taxpayer had not shown what different allocation should have been made. This action of the Board was correct, since it was incumbent upon the taxpayer not merely to show that the Commissioner's determination was erroneous, but to disclose sufficient facts from which a correct determination could be made. This well-settled rule applies to proceedings involving deficiencies

before the Board, as well as to suits to recover taxes unlawfully collected or withheld.

2. In cases coming from the Board of Tax Appeals the Circuit Courts of Appeals have power to remand only when the decision is not in accordance with law. Since, in the instant case, the Board reached the only possible decision on the record before it, the court below was without power except to affirm.

ARGUMENT

I

THE BURDEN ON THE TAXPAYER IS NOT ONLY TO PROVE THAT THE COMMISSIONER'S DETERMINATION IS ERRONEOUS, BUT TO SHOW THE CORRECT AMOUNT OF THE TAX

The question before the Circuit Court of Appeals in this case was whether the Board of Tax Appeals erred, as a matter of law, in approving the Commissioner's determination. If it did, the decision of the court below is correct; if the Board did not err, on the record before it, the Circuit Court of Appeals had power only to affirm.

It is the function of the Board of Tax Appeals to "redetermine the correct amount of the deficiency." Revenue Act of 1926, Section 274 (e) (U. S. C. App., Title 26, Sec. 1049 (a)), c. 27, 44 Stat. 9. Accordingly, where the Board decides that the Commissioner's determination is erroneous, its decision must determine what the correct

tax liability is. Therefore, it is apparent that the taxpayer's obligation goes beyond showing the Commissioner's determination to be erroneous; if the taxpayer stopped there, the Board would be unable to determine the correct tax. The presumption of correctness attaching to the Commissioner's determination does not disappear until the Board determines that the facts established satisfactorily overcome it. Further, in order to sustain his petition for redetermination, the taxpayer must show the correct amount of the tax. That this is true appears when it is considered that, from the beginning, the taxpayer is required to show the correct amount of tax and the facts upon which the tax is based. Sections 51 (a) and 54 (a) of the Revenue Act of 1928, *infra*, p. 28.

Since the establishment of the Board of Tax Appeals in 1924, it has been settled law that the burden of proof is on the petitioner. This arises both from the positive rule of the Board to this effect,[1] under its express authority to prescribe rules of evidence and procedure before it,[2] and from the long established rule that not only does a presumption of correctness accompany the Commissioner's determination but that, in order to set

[1] RULE 30. *Burden of Proof.*—The burden of proof shall be upon the petitioner, except as otherwise provided by statute and except that in respect of any new matter pleaded in his answer, it shall be upon the respondent.

[2] Sec. 900 (h) (U. S. C., Title 26, Sec. 1219), Revenue Act of 1924, c. 234, 43 Stat. 253.

it aside, the taxpayer must disclose facts necessary for a correct determination. See *United States* v. *Rindskopf,* 105 U. S. 418; *United States* v. *Anderson,* 269 U. S. 422, 443; *Reinecke* v. *Spalding,* 280 U. S. 227, 233.

Congress has recognized the existence of the general burden on the taxpayer before the Board by expressly excepting issues of fraud and transferee liability. Prior to the Revenue Act of 1928 even in these cases the burden rested upon the taxpayer to overcome the heavy presumption in favor of the Commissioner's determination. By that Act[3] it was definitely provided that, in any proceeding involving the issue whether the petitioner had been guilty of fraud with intent to evade the tax, the burden of proof on such issue should be on the Commissioner. And in transferee proceedings "before the Board the burden of proof shall be upon the Commissioner to show that a petitioner is liable as a transferee of property of a taxpayer, but not to show that the taxpayer was liable for the tax."[4]

The court below, however, has modified the rule as applied to the instant case. It has attempted to justify its action upon the ground that in proceedings on deficiencies before the Board, the bur-

[3] Sec. 601 (U. S. C. Sup. VII, Title 26, Sec. 612), Revenue Act of 1928, c. 852, 45 Stat. 791.

[4] Sec. 602 (U. S. C. Sup. VII, Title 26, Sec. 619), Revenue Act of 1928.

den on the taxpayer did not go so far as in the case of suits in the courts to recover taxes unlawfully collected or withheld, and further, that the rule in cases involving deductions was different from that in cases involving income items. It is submitted that the distinctions are not valid and that the rule of law is subject to no such modification.

No distinction has been made by this Court, or heretofore by the Circuit Courts of Appeals, in the application of the rule. In cases arising on deficiencies this Court has many times recognized and given effect to it. *Lucas* v. *Kansas City Structural Steel Co.*, 281 U. S. 264, 271; *Burnet* v. *Houston*, 283 U. S. 223, 227; *Phillips* v. *Commissioner*, 283 U. S. 589; *Welch* v. *Helvering*, 290 U. S. 111. In *Lucas* v. *Kansas City Structural Steel Co., supra*, involving an item of income as distinguished from a deduction, this Court said (p. 271):

> The Company's case falls far short of meeting the heavy burden of proving that the Commissioner's action was plainly arbitrary.

All of the Circuit Courts of Appeals have applied the rule to cases coming before the Board. Illustrative cases are compiled below.[5]

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[5] *DeFord* v. *Commissioner*, 29 F. (2d) 532 (C. C. A. 1st); *Darcy* v. *Commissioner*, 66 F. (2d) 581, 585 (C. C. A. 2d), certiorari denied, 290 U. S. 705; *Ruud* v. *Commissioner*, 45 F. (2d) 63 (C. C. A. 3d); *Anchor Co.* v. *Commissioner*, 42 F. (2d) 99 (C. C. A. 4th); *Avery* v. *Commissioner*, 22 F. (2d) 6 (C. C. A. 5th); *Louisville Cooperage Co.* v. *Commis-*

The Circuit Court of Appeals for the Second Circuit has itself often applied the rule which, we submit, is controlling here. In the recent case of *Darcy* v. *Commissioner,* 66 F. (2d) 581, 585, certiorari denied, 290 U. S. 705, which involved an addition to the taxpayer's gross income as distinguished from a claimed deduction, that court said (p. 585):

> The burden is upon the petitioners to show the correct amount of the tax in order to show that the commissioner's determination was wrong. Compare *Burnet* v. *Houston,* 283 U. S. 223, 228; 51 S. Ct. 413, 75 L. Ed. 991; *Reinecke* v. *Spalding,* 280 U. S. 227, 232, 233, 50 S. Ct. 96, 74 L. Ed. 385. In a situation like this, that requires proof that the amount of the deficiency is erroneous, for it is that fact, and not the method of computation, which controls.

And to the same effect are *Hubinger* v. *Commissioner,* 36 F. (2d) 724 (C. C. A. 2d), certiorari denied, 281 U. S. 741; *Sanderson* v. *Commissioner,* 42 F. (2d) 160 (C. C. A. 2d); *Autosales Corp.* v. *Commissioner,* 43 F. (2d) 931 (C. C. A. 2d); *Onondaga Co.* v. *Commissioner,* 50 F. (2d) 397 (C. C. A. 2d), certiorari denied, 284 U. S. 671.

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sioner, 47 F. (2d) 599 (C. C. A. 6th); *Commissioner* v. *Langwell Real Estate Corp.*, 47 F. (2d) 841 (C. C. A. 7th); *Twin City Tile & Marble Co.* v. *Commissioner*, 32 F. (2d) 229 (C. C. A. 8th); *Matern* v. *Commissioner*, 61 F. (2d) 663 (C. C. A. 9th); *Prey Bros. Live Stock Commission Co.* v. *Commissioner*, 36 F. (2d) 326 (C. C. A. 10th); *W. K. Henderson Iron Works & Supply Co.* v. *Blair*, 25 F. (2d) 538 (App. D. C.).

The instant case, in holding that the taxpayer was required to show only that the Commissioner's determination was incorrect, conflicts in principle with recent cases in other circuits which have applied the rule that the burden is on the taxpayer to show the correct amount of the tax in order to have the Commissioner's determination set aside. *Saxman Coal & Coke Co.* v. *Commissioner,* 43 F. (2d) 556 (C. C. A. 3d); *Williams* v. *Commissioner,* 45 F. (2d) 61 (C. C. A. 5th); *Alexander Sprunt & Son* v. *Commissioner,* 64 F. (2d) 424 (C. C. A. 4th); *Atlantic Bank & Trust Co.* v. *Commissioner,* 59 F. (2d) 363 (C. C. A. 4th); *Lightsey* v. *Commissioner,* 63 F. (2d) 254 (C. C. A. 4th); *Matern* v. *Commissioner,* 61 F. (2d) 663 (C. C. A. 9th). In the *Matern* case, which involved items of gross income, the court said (p. 666):

> Since the record here fails to supply information that enabled the Board of Tax Appeals to say that the Commissioner's determination was erroneous, or, if it was, to determine the correct amount of the tax, the board was bound to affirm the action of the Commissioner.
>
> In other words, the presumption of correctness is attached to the Commissioner's findings. The Board of Tax Appeals, after weighing the evidence, found that such evidence was not sufficient to rebut the presumption. The duty of weighing the evidence rests upon the board, and not upon

this court. Nevertheless, we are of the opinion that the board's view of the record was correct.

Williams v. *Commissioner, supra,* like the instant case, related to securities upon which the Commissioner had placed a different value than the taxpayer for purposes of establishing a gain.

The fact that a deficiency determined by the Commissioner is too great does not mean that the whole is erroneous; and the taxpayer is required to show in a proceeding before the Board how much of the deficiency is not due or that no deficiency is owing, for the same reason that in a suit for refund he must show that he is not liable for the whole or a part of the amount collected.

In *Atlanta Casket Co.* v. *Rose,* 22 F. (2d) 800 (C. C. A. 5th), it is stated that it is elementary, in suing to recover taxes, that the burden is on the plaintiff to allege and prove what the correct amount should be; and that it is immaterial what method the collector uses in making his assessment. If such be the rule, where the taxpayer is testing his liability for taxes by a suit to recover money claimed to have been wrongfully exacted from him as taxes, certainly it is not unreasonable to say that the same rule applies in a proceeding, likewise to test his liability for taxes, which was adopted solely for the benefit of the taxpayer to afford him an opportunity to be heard on the question of his liability without the necessity of prior payment of the amount claimed to be due from him.

In *Becker* v. *United States,* 21 F. (2d) 1003 (C. C. A. 5th), a suit was brought by the United States to recover the amount of an assessment which the taxpayer claimed to be erroneous. The court held that the taxpayer must show how much should be disallowed, since, upon proof that the assessment should be reduced by any particular amount, the Government would still be entitled to the remainder.

The court below stated that, if the burden of proof goes so far as to demand not only that the taxpayer show that the deficiency assessed against him is wrong, but what is the proper deficiency, or that there should be none at all, the decision was right, even though it appeared the tax was too high (R. 35).

It has been shown that the rule does go so far, and plainly so, as appears from its consistent application by this Court and by all the Circuit Courts of Appeals. It follows, therefore, that the Board of Tax Appeals rendered the only decision it could possibly have rendered upon the evidence before it, since there was no evidence to sustain a different determination.

That this is true appears from the Commissioner's determination and what the respondent established before the Board to refute it. The determination of the Commissioner was essentially not a valuation of property but an allocation—an apportionment between classes of stock of an aggre-

gate cost basis which is not disputed. The provisions of the statute and the regulations thereunder, Article 58, Treasury Regulations 74, *infra*, require only that a fair apportionment—not an exact one—be reached.

The respondent's only contention before the Board was that the cost basis assigned by the Commissioner to the preferred stock was too low; that of the admitted aggregate cost basis of the common and preferred stocks of $96,030, the whole of this sum should be apportioned to the preferred stock, since in his incorporation of his holding company he had arranged that it be entitled to cumulative dividends of $6 per share and to a priority of $100 per share on liquidation over the common. The respondent's whole effort and proof before the Board went on the theory that, if the total value of the assets acquired by the holding corporation did not at the time of such acquisition exceed the sum ($100,000) to which, by reason of its preference, the preferred stock was entitled upon liquidation, then it followed, as a matter of law, that neither class of common had any value and that, therefore, the total cost to respondent of the assets exchanged by him for such stock should be allocated in its entirety to the preferred. But such is not the case. The $48,771.16 assigned by the Commissioner to the preferred stock did not represent its value at date of acquisition by the taxpayer or at any other date, but only the proportionate part of the orig-

inal cost to the taxpayer of the stocks and assets of the operating companies. Even if the amounts used by the Commissioner in his formula for making the allocation were derived from values some eight months after the date of the exchange, and were thus improper elements because based upon conditions remote in time, the result reached by the formula may nevertheless have been correct. Furthermore, the amounts used were the only definite factors appearing in the record which might have been used to achieve a fair apportionment.

This Court, in a recent case, approved the use of a formula by the Commissioner to establish a basis for gain on sale of property. *Burnet* v. *S. & L. Bldg. Corp.*, 288 U. S. 406. There the court said (pp. 414, 415):

> The Commissioner's treatment of the excess of the mortgages on the 83rd Street property over the base cost followed the general purpose to place reasonable limitation upon the spread of the tax. It was appropriate in the unusual circumstances presented—certainly not prohibited. It was a practical way to accomplish the end. Some possible departure from the method prescribed for ordinary circumstances is not enough to destroy what he deemed necessary to meet unusual conditions.
>
> * * * * *
>
> The Commissioner and Board of Tax Appeals have practical knowledge of the intri-

> cate details incident to tax problems and their determination in circumstances like those under consideration here should be given effect when not clearly contrary to the will of Congress.

The applicable regulations, Article 58, *infra*, provide for apportionment except in cases where it is "impracticable." Unlike the instant case, *Kirkland* v. *Burnet*, 57 F. (2d) 608 (App. D. C.), relied upon by petitioner and the court below, is an example of where this is so. It was stipulated there that, at the time of purchase, it was "impracticable" to apportion the cost between the preferred and common stock. On this ground the court reversed the Board, without remanding for further hearing, and held the case was one precisely within the contemplation of Article 39, Treasury Regulations 65, which is substantially the same as Article 58, Treasury Regulations 74, *infra*, p. 30. The court below agreed (R. 35) that there was no showing here that allocation was impracticable.

This case does not present any unusual circumstances which, as suggested by the respondent, would justify or require that the burden of proof rule be relaxed. After the Board's decision, the taxpayer made an application for rehearing to enable him to present evidence as to the practicability of an allocation of cost, and, if practicable, the correct one. (R. 9.) This application was accompanied by affiidavits to the effect that the case was tried with the assent of counsel for the Commis-

sioner on a theory which did not demand an allocation. (R. 16.) The petition for rehearing was denied by the Board. (R. 2.) In the Circuit Court of Appeals the point was vigorously pressed but that court termed the affidavits "exceedingly vague and unsatisfactory", and refused to consider them. Furthermore, the Commissioner denied that he had ever agreed to the theory claimed by the taxpayer. In a case where it appeared that the Commissioner actually contributed to the taxpayer's failure to make proper proof, the Government sought no review. *Wyoming Investment Co.* v. *Commissioner,* 70 F. (2d) 191 (C. C. A. 10th).

II

IN THE ABSENCE OF ERROR THE CIRCUIT COURT OF APPEALS WAS WITHOUT POWER TO REMAND FOR FURTHER HEARING

If, as we contend, the Board properly affirmed on the ground that the taxpayer had not proved that the amount to be allocated to the preferred stock was any different from that determined by the Commissioner, there was no error of law in the Board's decision. The Circuit Courts of Appeals have no power to remand a case unless the decision of the Board is not in accordance with law. Revenue Act of 1926, Section 1003 (b), *infra,* p. 28. It has been so held in *Houston* v. *Commissioner,* 53 F. (2d) 445 (C. C. A. 3d), and *Thom* v. *Burnet,* 55 F. (2d) 1039 (App. D. C.), and the de-

cision of the court below in remanding the instant case to the Board for a new hearing is in conflict with those cases. This Court has similarly construed the power of a Circuit Court of Appeals to remand under R. S. 701, *Realty Acceptance Corporation* v. *Montgomery*, 284 U. S. 547.

The Circuit Court of Appeals for the Third Circuit correctly applied the rule in *Houston* v. *Commissioner, supra*, upon a mandate from this Court (*Burnet* v. *Houston*, 283 U. S. 223), to take such further proceedings in the case, in conformity with its opinion and judgment, as according to right and justice ought to be had. The Circuit Court of Appeals had reversed the Board on a finding by the latter that it was necessary for the taxpayer to show the March 1, 1913 value of certain property in order to establish the basis for a loss on its final disposition in 1920. The Circuit Court of Appeals held that only its cost in 1906 and the proceeds from its sale in 1920 were important. Upon review here, this Court in turn reversed the Circuit Court of Appeals and agreed with the Board that the 1913 value was a necessary element, that it was incumbent upon the taxpayer to prove that value as best he could, and that if it was impossible to prove that value, such a failure was a misfortune to be borne by the taxpayer as in other cases of failure of proof.

Upon remand to the Circuit Court of Appeals that court had before it the question of its power

to remand to the Board. The Commissioner challenged the court's right to remand for further hearing where the taxpayer had had one opportunity to prove his case but had failed to do so. The Circuit Court of Appeals considered the question carefully and held that, as the Board's decision was "in accordance with law" on the evidence presented before it, the court was without power to remand. It said (p. 448):

> They had their day in court and opportunity to submit evidence, if they had any, to establish this fact. They either could not produce such evidence or thought it was unnecessary. However that may be, the Board of Tax Appeals decided the case in accordance with the law as declared by the Supreme Court, and, its decision being "in accordance with law," we have never had power to remand the case. It follows that the petitions must be denied.

And in *Thom* v. *Burnet, supra,* in reply to the insistence of the taxpayer that the case be remanded to the Board for further hearing to determine the extent of worthlessness of a debt, the Court of Appeals for the District of Columbia said (p. 1040):

> For our jurisdiction to remand a case to the Board of Tax Appeals arises under the statute only if a case has been decided there "not in accordance with law." Section 1003 of the act (26 U. S. C. A., Sec. 1226). But as we are of opinion that the decision of this

> case by the Board of Tax Appeals was in accordance with law, it follows that we are without power to remand it for further proceedings. *Houston* v. *Commissioner of Internal Revenue* (C. C. A. 3d, 53 F. (2d) 445); * * *.

The Circuit Courts of Appeals review only errors of law committed by the Board of Tax Appeals, and the remanding of cases for further hearings should be confined to those cases where the Board has declined to admit pertinent evidence or has committed some other prejudicial error which could be corrected only by a rehearing. If there could be any doubt that this was the purpose of Congress it is completely dispelled by the legislative history of the Revenue Act of 1928, c. 852, 45 Stat. 791. The Revenue Bill of 1928 (H. R. No. 1, 70th Cong., 1st Sess.) in Section 601 proposed the amendment of Sections 906 and 907 (a) and (b) of the Revenue Act of 1924, c. 234, 43 Stat. 253. As proposed by the Bill, the amendment to Section 907 (b) contained the following language (p. 206):

> No decision of the Board shall be modified or reversed because the Board or any of its divisions has failed to consider evidence not adduced before the Board or division.

The explanation of this provision is found in the report of the Committee on Ways and Means of the House of Representatives (Report No. 2, 70th Cong., 1st Sess., pp. 30–31) which stated:

Sections 601 and 602 make a number of amendments with respect to the procedure of the Board of Tax Appeals.

* * * * *

Force and Effect of Rules.—A recent decision by the circuit court of appeals for the seventh circuit indicates that there is some disposition to regard the Board of Tax Appeals as an investigative rather than a judicial body, and to require it to reach its decisions not merely on the basis of the evidence presented in the record, but on the basis of such additional evidence outside the record as may be necessary fully to develop the taxpayer's case. The committee is of the opinion that the board's function is purely judicial, and in order to clarify the situation has provided that no decision of the board (whether rendered before or after the bill becomes law) should hereafter be modified or reversed because the board or any of its divisions has failed to consider evidence not adduced before the board or division. At the same time the committee has provided that the rules of practice and procedure of the board shall, just as the Federal equity rules, have the force and effect of law.

The provision proposed in the House Bill was subsequently stricken out. The omission is explained in the report of the Senate Committee on Finance (Report No. 960, 70th Cong., 1st Sess., p. 38), as follows:

Modification or reversal of board decision.—In view of certain expressions in a

> recent court opinion, the House bill in section 601 provides that no decision of the board shall be modified or reversed because the board has failed to consider evidence not adduced before it. While an appellate court has the right and duty, if an error of law has been made, to remand a case to the board for subsequent proceedings in accordance with law, the existing provisions of law clearly contemplate judicial, not administrative, procedure on the part of the board and the committee can see no need of further legislation on this subject. It is not the duty of the board to make investigations of tax cases but to decide the case on the basis of evidence properly placed before it by the commissioner and the taxpayer.

The court below apparently predicated its authority to remand the case upon its decision that the *finding of the Commissioner* was positively wrong. We have argued heretofore the finding was not plainly wrong but, even if it were, we submit that that fact alone would not justify the judgment of the court below. It was not the finding of the Commissioner which was being reviewed but a decision of the Board of Tax Appeals which although initiated upon a determination of the Commissioner, was made in a proceeding of a quasi-judicial character upon issues framed by the pleadings. If the decision of the Board of Tax Appeals was in accordance with law, the Circuit Court of Appeals had no authority to remand because of

error by the Commissioner. Many of the cases cited by the court below may be distinguished. Those that may be said to support the decision, we believe to be in error.

In *Collin* v. *Commissioner,* 32 F. (2d) 753 (C. C. A. 6th), the Commissioner, in computing the gain on the sale of stock, had allocated the entire cost of both preferred and common stock to the preferred. The court held that this action was not supported by the evidence and remanded the case for retrial. It will be noted that the court in this instance condemned the action of the Commissioner in attempting to do the very thing the respondent herein is urging should be done in his case.

Rhode Island Hospital T. Co. v. *Commissioner,* 29 F. (2d) 339, 342 (C. C. A. 1st), involved redetermination of a profits-tax deficiency, the Commissioner having denied an addition to reserves for bad debts for 1921. The court remanded for error of law because it plainly appeared that the Board had disregarded competent evidence.

In *Strother* v. *Commissioner,* 55 F. (2d) 626, 633 (C. C. A. 4th), a companion case of *Bankers Pocahontas Coal Co.* v. *Commissioner,* 287 U. S. 308, 309, it was conceded by counsel for the Commissioner in the Circuit Court of Appeals that the taxpayer could not reasonably be expected to maintain the complete burden of proof until the companion case was settled.

The evidence in *Underwood* v. *Commissioner,* 56 F. (2d) 67 (C. C. A. 4th), disclosed that the Commissioner had taxed the particular item of gross income there involved, and the Commissioner's action was sustained by the Board of Tax Appeals. The taxpayer contended that the item was not taxable. No question was presented to the Board that, if the item was taxable, it was subject to certain deductions. The Circuit Court of Appeals held that the Board was right in deciding that the item was taxable, but despite the fact that no issue as to deductions was presented to the Board and despite the fact that the Board had committed no error, the case was remanded for further hearing. In this we submit that the court exceeded its authority.

Eau Claire Book & Stationery Co. v. *Commissioner,* 65 F. (2d) 125 (C. C. A. 7th), is contrary to the established rule, but it appears that from the evidence before it the Board's action was probably arbitrary in disregarding evidence of value.

Ferguson v. *Commissioner,* 59 F. (2d) 893 (C. C. A. 10th), appears to have been remanded for further evidence because of an erroneous assumption by both parties as to a material fact. The court there said (p. 894):

> We feel certain that petitioner's loss was not compensated for by insurance, yet we doubt that we can take judicial notice of that fact; and conclude petitioner should have pleaded and proved it. However, since in the prior proceedings the parties appar-

> ently assumed that the loss was not compensated for and the Commissioner raises the question here for the first time, we are of the opinion that the case should be remanded to the Board with instructions to take evidence on the question of whether the loss was compensated for, and, if the Board finds it was not, to direct the allowance of the deduction.

The power conferred by the Revenue Act of 1926, *infra,* is one of review, not of appeal. The jurisdiction conferred is to affirm, or, if the decision of the Board is not in accordance with law, to modify or reverse such decision. But a finding on a question of value reached by the taxing officer or Board within the scope of the authority conferred by law, made in good faith, and in the absence of gross mistake or other irregularity, has long been held by the courts as conclusive. *Tracy* v. *Commissioner,* 53 F. (2d), 575, 578 (C. C. A. 6th), certiorari denied, 287 U. S. 632. There the court said (pp. 578, 579):

> But, whatever doubt there may have been as to the extent to which courts will accept the findings of fact of the Board of Tax Appeals, such doubts are laid at rest by the decision in the case of *Phillips* v. *Commissioner,* 283 U. S. 589, 600, 51 S. Ct. 608, 75 L. Ed. 1289. * * * This is but another way of saying that the decision of the taxing board must prevail if it is not contrary to the "indisputable character of the evidence" or if the evidence is "legally sufficient to sustain" such

finding. The evidence is legally sufficient to sustain the finding if there be substantial evidence to support it, and the record as a whole does not clearly, convincingly, or even possibly, "indisputably", require a contrary conclusion.

The statute was not designed to afford either the taxpayer or the Commissioner an additional opportunity to present evidence in support of their contentions. If the decisions relied upon by the respondent tend to support that view of the statute, it is submitted they are plainly wrong and contrary to the generally recognized rule—alike applicable to cases to recover taxes unlawfully collected or withheld and those involving deficiencies.

The effect of the decision below is uncertain, but it might be construed to impose upon the Commissioner the duty of proving on rehearing a new proposed deficiency—a difficult proposition, since the facts with respect to the valuation of assets and the income of the operating companies, which the court below suggested as a datum to arrive at the correct cost basis of the preferred stock, are peculiarly within the knowledge of the taxpayer and his associates. Conceivably, as a result of the court's decision, the Commissioner might have to make a series of subsequent determinations if the taxpayer shows that each is wrong without showing the correct amount—clearly an undesirable situation from the standpoint of efficient tax administration.

The rule that a presumption of correctness attaches to the Commissioner's determination, until sufficient facts are submitted by the taxpayer from which a correct determination may be made, is vitiated if the Circuit Courts of Appeals have power to require the Board to reopen cases after failure of such proof by the taxpayer upon the first trial. Taxpayers would be permitted to try their cases piecemeal, and no consistent rules of practice and procedure could be enforced by the Board.

CONCLUSION

The respondent had a full and fair hearing, without prejudicial error, before the Board of Tax Appeals. If the determination of the Commissioner was wrong, the taxpayer did not present sufficient facts from which a correct determination could be made, and thus failed to sustain the burden resting upon him. In these circumstances, it is respectfully submitted that the Circuit Court of Appeals was without power to remand this cause for further proceedings.

J. CRAWFORD BIGGS,
Solicitor General.
FRANK J. WIDEMAN,
Assistant Attorney General.
SEWALL KEY,
MAURICE J. MAHONEY,
Special Assistants to the Attorney General.

NOVEMBER 1934.

APPENDIX

Revenue Act of 1926, c. 27, 44 Stat. 9:

SEC. 1003. (a) The Circuit Court of Appeals and the Court of Appeals of the District of Columbia shall have exclusive jurisdiction to review the decisions of the Board (except as provided in section 239 of the Judicial Code, as amended); and the judgment of any such court shall be final, except that it shall be subject to review by the Supreme Court of the United States upon certiorari, in the manner provided in section 240 of the Judicial Code, as amended.

(b) Upon such review, such courts shall have power to affirm or, if the decision of the Board is not in accordance with law, to modify or to reverse the decision of the Board, with or without remanding the case for a rehearing, as justice may require. (U. S. C. App., Title 26, Sec. 1226.)

Revenue Act of 1928, c. 852, 45 Stat. 791, 807, 808:

SEC. 51. INDIVIDUAL RETURNS.

(a) *Requirement.*—The following individuals shall each make under oath a return stating specifically the items of his gross income and the deductions and credits allowed under this title * * *.

SEC. 54. RECORDS AND SPECIAL RETURNS.

(a) *By taxpayer.*—Every person liable to any tax imposed by this title or for the collection thereof, shall keep such records, render under oath such statements, make such

returns, and comply with such rules and regulations, as the Commissioner, with the approval of the Secretary, may from time to time prescribe. * * *

SEC. 111. DETERMINATION OF AMOUNT OF GAIN OR LOSS.

(a) *Computation of gain or loss.*—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the basis provided in section 113, and the loss shall be the excess of such basis over the amount realized.

* * * * *

(d) *Recognition of gain or loss.*—In the case of a sale or exchange, the extent to which the gain or loss determined under this section shall be recognized for the purposes of this title, shall be determined under the provisions of section 112. * * *

SEC. 113. BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Property acquired after February 28, 1913.*—The basis for determining the gain or loss from the sale or other disposition of property acquired after February 28, 1913, shall be the cost of such property; except that—

* * * * *

(6) *Tax-free exchanges generally.*—If the property was acquired upon an exchange described in section 112 (b) to (e), inclusive, the basis shall be the same as in the case of the property exchanged, decreased in the amount of any money received by the taxpayer and increased in the amount of gain or decreased in the amount of loss to the taxpayer that was recognized upon such exchange under the law applicable to the year in which the exchange was made. * * *

Treasury Regulations 74:

ART. 58. *Sale of stock and rights.* * * * Where common stock is received as a bonus with the purchase of preferred stock or bonds, the total purchase price shall be fairly apportioned between such common stock and the securities purchased for the purpose of determining the portion of the cost attributable to each class of stock or securities, but if that should be impracticable in any case, no profit on any subsequent sale of any part of the stock or securities will be realized until out of the proceeds of sales shall have been recovered the total cost. * * *

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No. 289

IN THE

Supreme Court of the United States

OCTOBER TERM, 1934.

GUY T. HELVERING, Commissioner of Internal Revenue,

Petitioner,

v.

WALTER W. TAYLOR.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR RESPONDENT IN OPPOSITION.

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ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR RESPONDENT IN OPPOSITION.

Opinions Below.

The opinion of the Board of Tax Appeals (R. 12) is unreported. The opinion of the Circuit Court of Appeals (R. 67) is reported in 70 F. (2d) 619.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered on May 18, 1934 (R. 70). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

Question Presented.

Whether, under the peculiar circumstances of this case, the Circuit Court of Appeals erred in remanding the case for further proceedings, where the Board of Tax Appeals had decided the Commissioner's determination of the taxpayer's income to be correct, despite the fact that such determination had been established to be wrong: that is to say,

Whether, where the Commissioner made a determination that the taxpayer's income be increased, and the taxpayer appealed to the Board of Tax Appeals, and at the trial, relying upon an agreement of counsel that proof of one issue would establish that his income should not be increased, confined his proof to that issue, and the Board thereafter decided that, for lack of further evidence, it could not determine whether, or in what amount, the taxpayer had additional income, the Circuit Court of Appeals erred in remanding the case to the Board for further proceedings when, despite the fact that such determination of the Commissioner was wrong on its face, and in any event was proven to be wrong by the evidence which was introduced, the Board both failed to require further evidence on its own motion, and refused to receive further evidence duly offered by the taxpayer in a motion for new trial (although such evidence, if adduced, would have established that the taxpayer had no additional income) but on the contrary, without attempting any decision on the merits, decided that the taxpayer had the additional income determined by the Commissioner.

Statutes and Regulations Involved.

The Statutes and Regulations involved are set out in the Appendix, *infra*, pp. 19, 20.

Statement.

The Board of Tax Appeals made no separate findings of fact and only a memorandum opinion. A statement of the substance of all the evidence adduced, agreed to by counsel for the Commissioner and duly settled by the Board, appears in the Record (R. 48-64).

In August, 1927, the taxpayer purchased, at a total cost of $96,030., all the stocks of three small public utilities companies and all the assets of an unincorporated fourth public utility enterprise, and thereupon, and on September 1, 1927 (R. 51) (and not on October 13, 1927, as stated in the petition and the Board's memorandum opinion), incorporated the Allied Public Service Corporation for the purpose of taking over said four public utilities. He thereupon incorporated the unincorporated public utility enterprise and thereupon, and on October 13, 1927, transferred the stocks of all four public utility companies to said Allied Public Service Corporation in a non-taxable exchange,[1] and received in return all the stock of that corporation, to wit: 1,000 shares $6. no par cumulative preferred, entitled to a prior $100. per share on liquidation and callable at $105.; 2,500 shares Class A Common, callable at $35.; and 5,000 shares Class B Common (R. 50, 51, 52, 57, 58). At the trial herein the taxpayer, who was the only witness called, was qualified as an expert witness (R. 49, 50, 56, 59, 61) and testified that the value of the stock of the Allied Public Service Corporation was no greater than the aggregate of the stocks of said four public

1. With the result that the taxpayer's cost basis for all the stock of the Allied Public Service Corporation was the same as the cost to him of the four small public utility companies.

utility companies, for the same were separated by other companies and could not be operated more economically, nor at a greater profit, nor were the same more readily salable, under one ownership than under four (R. 56, 59, 60, 61, 62); that beginning in the late winter of 1927 and running to and beyond May, 1928, a large appreciation took place in the market price of public utility stocks and properties (R. 55, 56, 57, 59, 60); that after making numerous unsuccessful attempts to sell the stocks of said four small public utility companies, said Allied Public Service Corporation was approached by a holding company which had an unusual need for properties of this precise size and location, which fortuitous circumstance, together with said appreciation, made it possible in May, 1928, for said Allied Public Service Corporation to sell said stocks for $194,930.16; and such sale was accomplished (R. 52, 53, 54, 55, 59, 61). Thereafter, and during the year 1928, the taxpayer sold his preferred stock in said Allied Public Service Corporation for $99,000. (R. 52).

In his income tax return for 1928, the taxpayer reported, as profit on such sale, the difference between $99,000., the sale price of the preferred and $96,030., the cost of all the stock (R. 52).[2]

The Commissioner, thereafter, issued his deficiency notice to the taxpayer in which he finally determined

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2. Applying the rule that where it is impracticable fairly to apportion, to the stock sold, a part of the cost of several classes of stock, acquired in a lump sum transaction, no profit is realized until, out of the proceeds, the total cost shall first have been realized; and that all the proceeds of the balance of the stock, when sold, constitutes income.

Regulations 74, Art. 58 (*infra*, p. 20).
Collin v. *Commissioner*, 32 F. (2d) 753.
Kirkland v. *Burnet*, 57 F. (2d) 608.

the taxpayer's cost basis for his said preferred stock to be $48,771.16, or that proportion of $96,030., the cost of all said stock, which was represented by a fraction, the denominator of which was $194,930.16, the price for which said Allied Public Service Corporation sold its said assets in May, 1928, and the numerator of which was $99,000., the sum for which the taxpayer thereafter sold his preferred stock (R. 52, 53). The taxpayer duly took his appeal, from said deficiency notice, to the Board of Tax Appeals (R. 4-10).

At the trial before the Board, counsel for the Commissioner and then counsel for the taxpayer orally agreed that if the value of all the assets of the Allied Public Service Corporation (consisting of said stocks of said four small public utility companies), at the time the same were acquired from the taxpayer, was not in excess of the cost of said assets to the taxpayer, or $96,030., then there was no deficiency. The Board Member conducting the trial inquired of counsel for the Commissioner if he concurred in this statement and counsel for the Commissioner stated that he concurred.

The said oral stipulation of counsel and question by the Board Member and answer by counsel for the Commissioner do not appear in the transcript of the proceedings at the trial, but that the same took place is established by the affidavit of William P. Jeffery (R. 35, 36) and one of the affidavits of Walter R. Bullock (R. 34) annexed to the motion for new trial and incorporated by reference in the Petition to the Circuit Court of Appeals praying for review of the decision of the Board.

Acting upon the faith of such agreement, the taxpayer introduced evidence only as to the value of said assets as of said date (R. 48-64).

Thereafter, the Board made its memorandum opinion (R. 12-18) and decision (R. 18) that however well the taxpayer had proven that the value of all the assets of the Allied Public Service Corporation, at the time the same were acquired by it, was only $96,030., still that was only one term, the denominator, of a correct fraction to apply, for purposes of apportionment, against the cost of all the stock; and that the taxpayer should have proven a proper numerator as well. The Board did not make any finding as to whether it was in fact practicable fairly to apportion the cost basis of all the stock, but decided that by introducing evidence only as to the value of said assets at said date, the taxpayer had failed to prove his case; and that the Commissioner's determination was entitled to a presumption of correctness and should be redetermined.

Thereafter, the taxpayer moved for a new trial (R. 19-37), contending that he should not be penalized for failing to introduce evidence as to other matters when he refrained from offering the same by reason of said oral stipulation of counsel; and further contending that in any event it is common knowledge, of which Courts have taken, and the Board should take, judicial notice that preferred and common stocks do not appreciate at the same rate and could not have done so in the circumstances here; that by virtue of that fact the Commissioner's said determination was wholly erroneous, arbitrary and fanciful on its face as a matter of law, for the same was based upon a 1928 ratio which was no evidence of the 1927 ratio but, rather, was conclusive evidence of what the 1927 ratio was not; that, therefore, the Commissioner's said determination was not entitled to any presumption of correctness and should not have been redetermined; and that the Board should grant a new trial at which to receive the evidence, de-

scribed in the supporting affidavits and offered for production, to show that no fair apportionment of said total cost was practicable as of the date of the acquisition of said stock by the taxpayer, and to enable the Board to decide the appeal on the merits.

The Board denied said motion from the bench (R. 2); and the taxpayer appealed to the Circuit Court of Appeals for the Second Circuit, which reversed and remanded (R. 67-70).

ARGUMENT.

I.

The questions presented in this cause are unique and not of general importance.

The questions presented in this case are not, it is submitted, capable of reduction to any such question of general import as contended in the petition. While a negative answer to the question propounded in the petition would, of course, result in affirmance here, a reversal would not necessarily follow from a decision that under normal circumstances a taxpayer before the Board of Tax Appeals has the burden of proving not only that the determination of the Commissioner is wrong but also what a correct determination should be.

The instant case is complicated by the stipulation of counsel that proof of one issue would establish the taxpayer's case. Where a case is tried upon such a state of facts, we submit that the taxpayer should, without more, be entitled to another opportunity to prove his case, when the Board decides, as here, after the close of the trial, that however well the fact in question was

proven, still sufficient facts upon which to base any decision have not been shown. The taxpayer, upon the Board's decision that all the necessary facts had not been proven, moved for a new trial offering additional evidence described in supporting affidavits. The additional evidence offered would have established that no allocation to the preferred of a part of the cost of all of the stock, was practicable; and hence that there was no deficiency. But the Board denied the motion and refused to accept the evidence. This action, in our view, injects a question, peculiar to this case, which might well be decisive.

Moreover, there can be no question of the taxpayer's burden of proof in this case, for the determination of the Commissioner from which the appeal to the Board was taken was wrong on its face and could have carried no presumption of correctness to raise any burden of proof on the taxpayer. The Commissioner's determination itself establishes its error. The taxpayer paid $96,030. for assets which he exchanged with all reasonable speed for all the common and preferred stock of a corporation which had no other assets. The preferred was no par, was callable at $105., and its total liquidation value was $100,000. Seven or eight months later the corporation sold the assets for $194,930.16 and the petitioner sold his preferred stock for $99,000., thus establishing $\frac{99,000}{194,930.16}$ as the ratio of the preferred to all the stock at the later date. But the Commissioner determined the ratio of the later date to be also the ratio of the earlier date, a determination, wrong on its face, for the common must have appreciated, during the interval, to a much greater extent than the preferred. The later ratio was not only no evidence of the earlier,

but was, on the contrary, conclusive evidence of the one ratio which could not have obtained at the earlier date.

The presumption of correctness of a determination by the Commissioner of Internal Revenue, which lays a burden of proof upon a taxpayer, is based upon a presumption of the exercise of sound discretion by the Commissioner, but where the Commissioner refuses or fails to exercise his discretion, or makes a determination which is no more than capricious or fanciful, no presumption of correctness can arise. It is a mere contradiction in terms to say that a determination, wrong upon its face, is presumptively correct. The rule as to burden of proof in a normal case, where the Commissioner's determination is entitled to a presumption of correctness, cannot be involved in this case which is fundamentally abnormal.

In view of the unique questions involved in this case, it is submitted that a review thereof would be limited to a consideration of the merits and would not require the decision of any question of general importance.

II.

The decision below appears to be correct.

The decision of the Circuit Court of Appeals in remanding this case for findings of fact upon which a decision on the merits could be made is not one which involves unfairness to the Government; the Court could well have decided from the record that there was no deficiency.

The record contains sufficient evidence to have served as a basis for a decision that no allocation was prac-

ticable. The taxpayer acquired all the stock of the Allied Public Service Corporation. The record discloses that he held the preferred throughout the period in question, and nothing appears to rebut the presumption that he continued to hold all the common. No sales or other evidence of respective values for the different classes of stock were suggested in the respondent's determination or otherwise. No dividends were distributed by the underlying companies at any time while they were under the control of the taxpayer (R. 62).[3] The record does not contain a statement of the financial histories of the four underlying companies, but the Commissioner had this information, for he had their income tax returns. The Commissioner had fully audited the taxpayer's return and examined his books and records. He had sent the taxpayer two audit letters proposing additional tax and had received the taxpayer's statements in protest. The Commissioner was in possession of all the facts and must be presumed to have made the best allocation that could be made. When that allocation proves to be wrong on its face, it must amount, it is submitted, to an admission that no allocation was practicable. In remanding the case for further proceedings the Circuit Court of Appeals did not deviate from the most scrupulous fairness to the Government.

Nor was the technical ground of the taxpayer having met his burden of proof, the only ground upon which the Circuit Court of Appeals might have remanded. That decision would have been amply justified upon the single ground that the petitioner was entitled to an opportunity to present his further evidence, inasmuch as it was withheld at the trial in reliance upon the

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3. Although in its memorandum opinion the Board stated that there was no testimony of this fact (R. 17).

stipulation of counsel that only one fact need be proved; or upon the single ground that the evidence described and offered in the motion for new trial would have established no deficiency to be due, and that justice is not to be defeated by a mistake or misfortune at the trial.

But aside from all the above and considering the matter only from the point of view of the question stated in the petition to be raised by the case, the Circuit Court of Appeals could hardly have failed to reverse and remand.

The rule is uniform and well settled that where, in a proceeding before the Board of Tax Appeals, the determination of the Commissioner has, as here, been established to be wrong, but, evidence sufficient to form a basis for a decision on the merits not having been introduced, the Board has redetermined the erroneous determination of the Commissioner, the decision of the Board will be reversed and the case sent back for further facts. The Circuit Courts of Appeals for every circuit and the Court of Appeals of the District of Columbia have so held.[4]

Rhode Island Hospital Trust Co. v. *Commissioner* (C. C. A. 1) 29 F. (2d) 339;

Conrad & Co., Inc. v. *Commissioner* (C. C. A. 1) 50 F. (2d) 576;

Cohan v. *Commissioner* (C. C. A. 2) 39 F. (2d) 540;

Pittsburgh Hotels Co. v. *Commissioner* (C. C. A. 3) 43 F. (2d) 345;

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4. Except that in the Third Circuit the Court has gone farther and laid down the rule that where the Commissioner's determination is shown to be wrong, the Commissioner must show why the return should not be approved.

Nichols v. *Commissioner* (C. C. A. 3) 44 F. (2d) 157;
Strother v. *Commissioner* (C. C. A. 4) 55 F. (2d) 626, aff'd. 287 U. S. 308;
Underwood v. *Commissioner* (C. C. A. 4) 56 F. (2d) 67;
Independent Ice & Cold Storage Co. v. *Commissioner* (C. C. A. 5) 50 F. (2d) 31;
Collin v. *Commissioner* (C. C. A. 6) 32 F. (2d) 753;
Eau Claire Book & Stationery Co. v. *Commissioner* (C. C. A. 7) 65 F. (2d) 125;
Kendrick Coal & Dock Co. v. *Commissioner* (C. C. A. 8) 29 F. (2d) 559;
Citrus Soap Co. of California v. *Lucas* (C. C. A. 9) 42 F. (2d) 372;
Ferguson v. *Commissioner* (C. C. A. 10) 59 F. (2d) 893;
Kirkland v. *Burnet* (C. A., D. C.) 57 F. (2d) 608;
Dempster Mill Mfg. Co. v. *Burnet* (C. A., D. C.) 46 F. (2d) 604.

It is difficult to see how the rule could be otherwise.

In the instant case, if, for purposes of the point, we concede that there was nothing in the record upon which a decision of no deficiency could have been based, the Board, after the trial, and without the further evidence offered, could not have known whether or not the taxpayer had any additional income, or, if so, in what amount. There was only one fact of which the Board could have been certain, and that was the fact that the taxpayer did not have the additional income which the Commissioner had determined. To ask for a reversal of the decision of the Circuit Court of Appeals

in this case, the Commissioner must contend that the Board should be upheld in deciding that the taxpayer did receive the one item of income which it knew he did not receive. A contention that any determination of the Commissioner, even though it be that two plus two equals five, is nevertheless entitled to a presumption of correctness, seems equally impossible of support. Yet these are the positions which must, it is submitted, be taken and sustained by the Commissioner in order to ask for a reversal here.

That the determination of the Commissioner in this case was wrong on its face seems too clear for serious contradiction. Assets were purchased in August by the taxpayer for $96,030. He transferred them on October 13 to a corporation, which had no other assets, for all its stock, common and preferred. In May of the following year the assets were sold for $194,930.16. At that time the ratio of the preferred to all the stock was $\frac{99,000}{194,930.16}$. The Commissioner determined the same ratio to have obtained at the date of the transfer to the corporation by the taxpayer. On its face the determination was wrong, for at least part of the appreciation must have taken place during the interim, and common and preferred stocks do not appreciate at the same rate.[5]

When, however, the proof made at the trial is taken into consideration, the error of the Commissioner's determination is made even more certain.

No contention made on behalf of the Commissioner goes so far as to allege that the determination made by him in this case was correct, but the petition does contend that it was not necessarily wrong. It is submitted,

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5. The Court of Appeals of the District of Columbia took judicial notice of this fact in *Kirkland* v. *Burnet, supra.*

however, that the point made in the petition in this respect is based upon erroneous premises.

In this regard the petition urges that at least a part of the appreciation had taken place between the purchase of the four original properties and the transfer to the holding company. The taxpayer bought the original properties in August, 1927 (R. 50) and thereupon and on September 1, 1927 (R. 51) formed the holding company. One of the original companies, which was unincorporated, was then incorporated; and the stocks of the four were transferred to the holding company, and its stock issued to the taxpayer, on October 13, 1927. It is submitted that, in the circumstances, this acquisition should relate back, for the taxpayer bought the original properties for the purpose of transferring them to the holding company. But in any event, the petition is in error in assuming any appreciation to have taken place prior to, or upon, the acquisition by the holding company. Quite the contrary, the uncontradicted testimony of the taxpayer, who was the only witness, and who was qualified as an expert was, as above set out in the statement of the case, that the stock of the holding company was of no greater value than the aggregate value of the stocks of the four original properties. The original properties were not contiguous (except for the two which cost $9,500. and $4,500., respectively) and none of the economies of operation or other advantages of combination referred to in the petition occurred (R. 56, 59, 60, 61, 62). The appreciation took place in the winter of 1927 and the spring of 1928 (R. 55, 56, 57, 59, 60), and the price at which the properties eventually sold was due to such appreciation and to fortuitous circumstance (R. 52, 53, 54, 55, 59, 61).

While, as aforesaid, the entire appreciation took place between October 13, 1927 and May, 1928, that fact is not essential to show the absolute error of the Commis-

sioner's determination. So long as any substantial part of the appreciation took place between those dates, and this the petition does not attempt to deny, the later ratio must have been different from the earlier. The total assets of the corporation being substantially equal to (or even if they had been in excess of) the liquidation value of the preferred at the earlier date, it seems impossible to contend that the appreciation in the assets did not effect a greater increase in the value of the common than in the value of the preferred.

The determination of the Commissioner was wrong on its face, and in any event was proven to be wrong. If, in spite of the self-demonstrated error of the Commissioner's determination, it was entitled to any presumption, the taxpayer had rebutted it. The decision of the Board was that the taxpayer had received income which, it had been established, he had not received. By reversing that decision, and remanding the case, the Circuit Court of Appeals did not impose any duty upon the Commissioner to prove a new proposed assessment, nor did it even impose upon the Board, as a fact finding body, the duty of requiring further evidence. The evidence of the facts necessary to make a decision on the merits is available and has been offered by the taxpayer and refused by the Board. That evidence would establish that the additional tax which has been assessed against and collected from the taxpayer was not due.

The decision of the Court below appears to be right.

III.

There does not appear to be any conflict.

The principal ground upon which the petition asks that certiorari issue is an asserted conflict between the decision in this case and the decisions of certain of the

Circuit Courts of Appeals cited in the petition. But the contention that the cases cited in the petition establish a rule that the burden is on the taxpayer to show the correct amount of the tax in order to have the Commissioner's determination set aside, will not, it is submitted, survive a close inspection.

In our view, none of the cases cited lays any heavier burden upon a taxpayer before the Board than to disprove the Commissioner's determination. In some cases the Courts have indeed used language on its face indicative of a further duty, but it is submitted that such language results from the fact that the most feasible disproof of one fact is, oftentimes, proof of a contrary fact. That such is the meaning of the language used is exemplified by the extract from the opinion in *Darcy, et al.* v. *Commisioner,* (C. C. A. 2) 66 F. (2d) 581, 585, cert. den. 290 U. S. 705, quoted in the petition as follows:

> "The burden is upon the petitioners to show the correct amount of the tax *in order to show that the commissioner's determination was wrong.* * * *" (Italics supplied).

In all the cases cited in the petition for this point (except *Becker* v. *U. S.*, [C. C. A. 5] 21 F. [2d] 1003),[6] the Board was upheld in redetermining the determination of the Commissioner for lack of proof by the tax-

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6. In this case the taxpayer had reported its income on the cash basis, which did not correctly reflect income. The Commissioner made an assessment on the accrual basis, which, although not exact, was "as nearly accurate as it was possible to make from the company's books". The taxpayer apparently contented itself with a general contention for the cash basis and the Court approved the assessment. This case presented a special situation; and the same Court subsequently decided *Independent Ice & Cold Storage Co.* v. *Comm., supra,* without reference to it. In any event the *Becker* case did not involve a proceeding before the Board.

payer. But despite the language of the respective Courts relied on in the petition, the fact is that in those cases the taxpayers had not only failed to prove the correct amount of the tax, but had also failed to prove that the Commissioner's determination was wrong.

The cases cited in the petition, then, stand for no more than the proposition, which no one would question, that a taxpayer before the Board has the burden of proving the Commissioner's determination to be wrong. Those cases, it is submitted, are not in conflict with—they are complementary to—the cases hereinabove cited which hold that the Board may not redetermine a determination made by the Commisioner, but established to be wrong. That this construction is correct is amply attested by the fact that, as aforesaid, the Circuit Courts of Appeals of every circuit and the Court of Appeals of the District of Columbia have decided that where the Commissioner's determination has been established to be wrong, the Board may not redetermine it. Indeed in the ninth circuit, *Matern* v. *Commissioner*, (C. C. A. 9) 61 F. (2d) 663, cited in the petition as holding that the taxpayer must show the correct amount of tax, has been cited in a later case by the same Court for the proposition that:

> "This court has held that 'the presumption of correctness is attached to the Commissioner's findings'. *Matern* v. *Comm'r.*, 61 F. (2d) 663, 666. So from the outset the determination by the Commissioner of the fair market value of the property in question was *prima facie* correct and the burden of establishing it as incorrect was upon the petitioner."
>
> *Old Mission Portland Cement Co.* v. *Commissioner*, (C. C. A. 9) 69 F. (2d) 676, 679.

Nor do the cases holding that a taxpayer suing for a refund must prove the correct tax establish a conflict. In those cases the taxpayer is the plaintiff in a suit for a money judgment. He must prove the amount by which his tax has been overpaid, and to do this must, of course, prove the correct amount of the tax.

Even on the question stated in the petition to be presented here, there appears to be no conflict.

Conclusion.

In conclusion it is respectfully submitted that the petition for certiorari should be denied, for:

(a) There is no conflict in respect of the question propounded in the petition;

(b) Whether or not there is such a conflict, this case is so unique that neither that question nor any other question of general importance is raised;

(c) In any event the decision of the Court below is clearly right, for the decision of the Board was wrong and the evidence upon which to base a decision on the merits was, and is, available and in justice ought to be received.

Respectfully submitted,

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26 Liberty St.,
New York, N. Y.

Dated, New York, N. Y., September 6, 1934.

APPENDIX.

Revenue Act of 1926, c. 27, 44 Stat. 9, 110:

Sec. 1003. (a) The Circuit Courts of Appeals and the Court of Appeals of the District of Columbia shall have exclusive jurisdiction to review the decisions of the Board (except as provided in Section 239 of the Judicial Code, as amended); and the judgment of any such court shall be final, except that it shall be subject to review by the Supreme Court of the United States upon certiorari, in the manner provided in Section 240 of the Judicial Code, as amended.

(b) Upon such review, such courts shall have power to affirm or, if the decision of the Board is not in accordance with law, to modify or to reverse the decision of the Board, with or without remanding the case for a rehearing, as justice may require. (U. S. C. A., Title 26, Sec. 1226.)

Revenue Act of 1928, c. 852, 45 Stat. 791, 815, 818:

Sec. 111. Determination of Amount of Gain or Loss. (a) *Computation of gain or loss.*—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the basis provided in Section 113, and the loss shall be the excess of such basis over the amount realized.

* * * * *

(d) *Recognition of gain or loss.*—In the case of a sale or exchange, the extent to which the gain or loss determined under this section shall be recog-

nized for the purposes of this title, shall be determined under the provisions of Section 112.

* * * * *

Sec. 113. BASIS FOR DETERMINING GAIN OR LOSS. (a) *Property acquired after February 28, 1913.*—The basis for determining the gain or loss from the sale or other disposition of property acquired after February 28, 1913, shall be the cost of such property; except that—

* * * * *

(6) *Tax-Free Exchanges Generally.*—If the property was acquired upon an exchange described in Section 112 (b) to (e), inclusive, the basis shall be the same as in the case of the property exchanged, decreased in the amount of any money received by the taxpayer and increased in the amount of gain or decreased in the amount of loss to the taxpayer that was recognized upon such exchange under the law applicable to the year in which the exchange was made. * * *

Treasury Regulations 74:

Art. 58. *Sale of stock and rights.*—* * * Where common stock is received as a bonus with the purchase of preferred stock or bonds, the total purchase price shall be fairly apportioned between such common stock and the securities purchased for the purpose of determining the portion of the cost attributable to each class of stock or securities, but if that should be impracticable in any case, no profit on any subsequent sale of any part of the stock or securities will be realized until out of the proceeds of sale shall have been recovered the total cost.

* * * * *

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No. 289.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1934.

GUY T. HELVERING, Commissioner of Internal Revenue,

Petitioner,

v.

WALTER W. TAYLOR.

ON A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR THE RESPONDENT.

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WALTER W. TAYLOR.

ON A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

BRIEF FOR THE RESPONDENT.

Opinions Below.

The opinion of the Board of Tax Appeals (R. 6) is unreported. The opinion of the Circuit Court of Appeals (R. 33) is reported in 70 F. (2d) 619.

Jurisdiction.

The judgment of the Circuit Court of Appeals was entered on May 18, 1934, (R. 36). The petition for a writ of certiorari was filed August 14, 1934, and was granted October 8, 1934. The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code as amended by the Act of February 13, 1925.

Questions Presented.

Whether the Commissioner's determination that the taxpayer had additional income was wrong on its face,

and whether the decision of the Board of Tax Appeals was wrong in law in approving that determination.

Whether the circumstances relating to the theory upon which the case was tried in the Board of Tax Appeals constituted reversible irregularity.

Whether the taxpayer introduced competent evidence tending to show both that he did not have the additional income determined by the Commissioner, and that he had no additional income; and whether the decision of the Board of Tax Appeals was wrong in law in disregarding such evidence.

If the answers to all of the foregoing are in the negative, then whether the Circuit Court of Appeals erred in remanding this case to the Board of Tax Appeals for a new hearing, on the ground that the amount of income determined by the Commissioner and approved by the Board was incorrect.

Statutes and Regulations Involved.

The Statutes and Regulations involved are set out in the Appendix, *infra*, pp. 28-30.

Statement.

The Board of Tax Appeals made no separate findings of fact and only a memorandum opinion. A statement of the substance of all the evidence adduced, agreed to by counsel for the Commissioner and duly settled by the Board, appears in the record (R. 23-32).

In August, 1927, the taxpayer purchased, at a total cost of $96,030, all of the stocks of three small public utility operating companies and all of the assets of an unincorporated fourth public utility operating company,

and thereupon, and on September 1, 1927 (R. 25) (and not on October 13, 1927, as stated in the Board's memorandum opinion), incorporated the Allied Public Service Corporation as a holding company, to take over said four operating companies. He thereupon incorporated the unincorporated operating company, and thereupon, and on October 13, 1927, transferred the stocks of all four operating companies to said Allied Public Service Corporation, the holding company, in a non-taxable exchange,[1] and received in return all the stock of that corporation, to wit: 1,000 shares $6 no-par cumulative preferred, entitled to a prior $100 per share on liquidation and callable at $105; 2,500 shares Class "A" Common, and 5,000 shares Class "B" Common (R. 24, 25, 28). At the trial herein the taxpayer, who was the only witness called, was qualified as an expert witness (R. 24, 28, 29, 30), and testified that the value of the stock of the holding company was no greater than the aggregate of the stocks of said four operating companies, for the same were separated by other companies and, for that and other reasons, could not be operated more economically, nor at a greater profit, nor were the same more readily salable, under one ownership than under four (R. 27, 28, 29, 30, 31); that beginning in the late winter of 1927 and running to and beyond May, 1928, a large appreciation took place in the market price of public utility stocks and properties (R. 27, 28, 29, 30); that after making numerous unsuccessful attempts to sell the stocks of said four operating companies, said holding company was approached by another company which had an unusual need for properties of this precise size and location, which circumstance, together with said appre-

1. With the result that the taxpayer's cost basis for all the stock of the Allied Public Service Corporation was the same as the cost to him of the four small public utility companies.

ciation, made it possible in May, 1928, for said holding company to sell said stocks for $194,930.16; and such sale was accomplished (R. 25, 26, 27, 29, 30). Thereafter, and during the year 1928, the taxpayer sold his preferred stock in said holding company to that corporation for $99,000 (R. 25, 26).

In his income tax return for 1928, the taxpayer reported, as profit on such sale, the difference between $99,000, the sale price of the preferred, and $96,030, the cost of all of the stock (R. 26).

The Commissioner, thereafter, issued his deficiency notice to the taxpayer in which he finally determined the taxpayer's cost basis for his said preferred stock to be $48,771.16, or that proportion of $96,030, the cost of all of said stock, which was represented by a fraction the denominator of which was $194,930.16, the price for which said holding company sold the stocks of the operating companies in May, 1928, and the numerator of which was $99,000, the sum for which the taxpayer thereafter sold his preferred stock (R. 26). The taxpayer duly took his appeal, from said deficiency notice, to the Board of Tax Appeals (R. 2-6).

At the trial before the Board, counsel for the Commissioner and then counsel for the taxpayer orally agreed that if the value of all of the assets of the holding company (consisting of said stocks of said four operating companies), at the time the same were acquired from the taxpayer, was not in excess of the cost of said assets to the taxpayer, or $96,030, then there was no deficiency. The Board Member conducting the trial inquired of counsel for the Commissioner if he concurred in this statement and counsel for the Commissioner stated that he concurred.

The said oral stipulation of counsel and question by the Board Member and answer by counsel for the Commissioner do not appear in the transcript of the pro-

ceedings at the trial, but that the same took place is established by the affidavit of the taxpayer's counsel before the Board, William P. Jeffery (R. 17, 18), and one of the affidavits of taxpayer's accountant, Walter R. Bullock (R. 17), annexed to the motion for new trial and incorporated by reference in the petition to the Circuit Court of Appeals praying for review of the decision of the Board.

In accordance with such agreement, the taxpayer introduced only evidence addressed to proving the value of said assets as of said date (R. 23-32).

Thereafter, the Board made its memorandum opinion (R. 6-9) and decision (R. 9) that however well the taxpayer had proven that the value of all the assets of the Allied Public Service Corporation, at the time the same were acquired by it, was only $96,030, still that was only one term, the denominator, of a correct fraction to apply, for purposes of apportionment, against the cost of all of the stock; and that the taxpayer should have proven a proper numerator as well. The Board did not make any finding as to whether it was in fact practicable fairly to apportion the cost basis of all of the stock, but decided that because he had not shown any allocation different from that determined by the Commissioner, the taxpayer had failed to prove his case; and that the Commissioner's determination should, therefore, be approved.

Thereafter, the taxpayer moved for a new trial (R. 9-18), contending that he should not be penalized for failing to introduce further evidence when he refrained from offering the same by reason of said oral stipulation of counsel; and further contending that in any event it is common knowledge, of which Courts have taken, and the Board should take, judicial notice that preferred and common stocks do not appreciate at the same rate and could not have done so in the cir-

cumstances here; that by virtue of that fact the Commissioner's said determination was wholly erroneous, arbitrary and fanciful on its face as a matter of law, for the same was based upon a 1928 ratio which was no evidence of the 1927 ratio, but, rather, was conclusive evidence of what the 1927 ratio was not; that, therefore, the Commissioner's said determination was not entitled to any presumption of correctness and should not have been approved; and that the Board should grant a new trial at which to receive the evidence, described in the supporting affidavits and offered for production, to show that no fair apportionment of said total cost was practicable as of the date of the acquisition of said stock by the taxpayer, and to enable the Board to decide the appeal on the merits.

The Board denied said motion from the bench (R. 2); and the taxpayer appealed to the Circuit Court of Appeals for the Second Circuit, which reversed and remanded (R. 33-37).

Summary of Argument.

In this case the Government does not seriously contend that an additional tax in any such amount as that which has been collected from the taxpayer, was due on the merits. The Government does contend that even though the taxpayer had proved that he did not owe an additional tax so large as that asserted against him, the Board, nevertheless, committed no error in deciding that he owed the asserted tax. In support of this, the Government urges that the taxpayer was under the burden of proving not only that he did not owe the tax asserted, but also what his correct tax liability was; and in order to apply that proposition to this case,

assumes (without demonstrating) that the taxpayer failed to prove that he owed no additional tax.

While the Government cites no case holding a taxpayer's burden of proof to be so heavy, we contend that the fundamental fallacy in the Government's position lies in the assumption that this case involves that question.

In the first place, the Commissioner's determination was wrong on its face, and not entitled to any presumption of correctness, so that no question of burden of proof could arise. Again, the conduct of the trial upon the agreed but erroneous theory upon which the case was tried, constituted irregularity which should be corrected by rehearing.

Finally, and, as we submit, conclusively, the taxpayer did not fail in his proof either as to proving the Commissioner's determination to be wrong, or as to proving no additional tax to be due.

ARGUMENT.

I.

The determination of the Commissioner was wrong on its face and entitled to no presumption of correctness; and, in any event, was proven to be wrong by the evidence introduced.

In the year 1928 the taxpayer sold certain preferred stock for $99,000, and the question herein is the cost basis to be used by him in computing his profit on said sale. Said preferred stock was acquired by the taxpayer, together with all of the common stock in the same corporation, for $96,030 in a lump sum transac-

tion without any allocation of the total cost between the common and preferred.

The Statute, as pointed out in the opinion below, contains no provision for an allocation of cost in the event of partial realization, but the Commissioner has promulgated a Regulation which prescribes that where common stock is received as a bonus with a purchase of preferred, the total price shall be fairly apportioned between the respective classes, but that if such fair apportionment be impracticable in any case, no profit upon any sale of any of the stock is realized until the total cost shall have been first recovered.

If this Regulation does not state the law as applicable to this case, then the taxpayer, by proving the total cost, and the sale price of the preferred, has unquestionably proven that he did not owe the tax asserted against him and also that he did not owe any additional tax.

If the Regulation referred to does state the law as applicable to this case, then the first question to be determined is whether it was practicable fairly to apportion a part of the cost of all of the stock to the preferred, and, if so, then what part of such cost should be so apportioned. It has been held by the Circuit Courts of Appeals and the Board of Tax Appeals that the Regulation referred to states the law as applied to cases such as this.[2]

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2. Regulations 74, Art. 58, *infra* p. 29;
Collin v. *Commissioner*, 32 Fed. (2d) 753 (C. C. A. 6);
Kirkland v. *Burnet*, 57 Fed. (2d) 608 (App. D. C.);
Texas Penn Oil Co. v. *Commissioner*, 28 B. T. A. 917;
Hemphill v. *Commissioner*, 25 B. T. A. 1351.

In August, 1927, the taxpayer purchased four small public utility companies.[3] On September 1, 1927, he organized a holding company, and, having in the meantime incorporated one of the operating companies, which had been unincorporated, he conveyed the stocks of the four to the holding company and received all of its stock in exchange on October 13, 1927. This stock consisted of 1,000 shares of no-par preferred and 7,500 shares of no-par common. The preferred was entitled to cumulative dividends of $6 per share, was callable at $105, and was entitled to a prior $100 per share, or a total of $100,000, on liquidation.

In order to make an allocation to the preferred of a part of the cost of all of the stock, the respective values of the preferred, and of all the stock, as of the date of the taxpayer's acquisition thereof, must be found. The purchase of the four small operating companies and the transfer of their stocks to the holding company in exchange for all of its stock having been one continuous transaction, and the taxpayer having been the sole stockholder throughout, his acquisition of the stock of the holding company relates back to the acquisition of the operating companies. The operating companies were purchased for a total consideration of $96,030 in arms' length transactions (R. 24), and this established the value of all of the stock of the holding company as of the date of acquisition thereof by the taxpayer, and, consequently, established a denominator for a fraction of allocation to be applied against the same amount of $96,030 to determine what proportion thereof was properly allocable to the preferred stock as its cost basis.

But no numerator for such a fraction can be found.

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3. Although both the Government's brief and the opinion of the Board state that the taxpayer had theretofore acquired options, such statements are without any foundation in the evidence.

The Commissioner, who had audited the taxpayer's, and the holding company's, records and return, had full knowledge of all of the facts. He knew that there were no sales of any of the stock of the holding company at any time prior to the sale of the preferred, and that the operating companies had declared no dividends. Moreover, he had the returns of the operating companies themselves, and therefore knew their full financial histories. But the Commissioner was unable to find, and, as we submit, the record discloses that there cannot be found, a numerator for such a fraction.

In spite of the fact that it was apparent that no fair allocation was practicable, the Commissioner, nevertheless, purported to make an allocation. In May, 1928, the holding company sold the stocks of the operating companies, which had been worth a total of $96,030 at the date of the taxpayer's acquisition of the stock of the holding company, for $194,930.16, thus establishing that amount as the value of all of the stock of the holding company as of that date, and, consequently, as a denominator for a fraction which, if supplied with a proper numerator, would state the proportionate value of the preferred to all of the stock as of that time. The sale of the stock of the operating companies by the holding company was followed by the sale by the taxpayer of his preferred stock for $99,000, and thus the proportionate value of the preferred to all of the stock was established, as of that date, as $\frac{99,000}{194,930.16}$. That ratio had no relation to a fair allocation as of the date of the taxpayer's acquisition of the stock of the holding company, but the Commissioner, nevertheless, purported to determine that the ratio between the preferred and all of the stock as of that date was the same as the ratio as of May, 1928, or $\frac{99,000}{194,930.16}$.

In this, the Commissioner committed an error of law, for not only was the ratio of 1928 no evidence of the 1927 ratio, but, on the contrary, the later ratio was conclusive evidence of what the ratio of 1927 was not.

Kirkland v. *Burnet,* 57 F. (2d) 608 (App. D. C.).

The Government does not question the correctness of the holding of the *Kirkland* case that common and preferred stocks do not appreciate at the same rate. Yet that case involved precisely the same question as the instant case, except that there it was stipulated that if the later ratio could not be said to establish the earlier, then it was impracticable to establish the earlier ratio. The Government mentions that stipulation as a controlling distinction, but it is submitted that the distinction is merely between the relief appropriate in that case and this. There the Court properly reversed without remanding. Here, the Court held the evidence of impracticability of apportionment not to be sufficiently conclusive to enable it to reverse without remanding.

The taxpayer's contention is not, as suggested in the Government's brief, simply that neither the value of $99,000, for the preferred, nor $194,930.16 for all of the stock, had any relation to the date of acquisition by the taxpayer of his stock in the holding company, although, of course, such is the case; we urge that the increase in the value of the assets of the holding company from $96,030 to $194,930.16 must have resulted in a much greater increase in the value of the common, than in the preferred. At the earlier date the total assets of the corporation were insufficient either to retire the preferred or to satisfy it upon liquidation. At that time, if, for purposes of the point, we concede any value to the common, it must have been not only un-

ascertainable, but in any event very small. At the later date, on the other hand, the assets of the corporation were sufficient to have retired the preferred, or satisfied it on liquidation, and still leave nearly as much again for the common.

There is no scintilla of evidence in the record tending to show that the ratio of the preferred to all of the stock of the holding company at the date of the taxpayer's acquisition thereof, was $\frac{99,000}{194,930.16}$, as decided by the Board. The evidence did establish $\frac{99,000}{194,930.16}$ to be the ratio as of May, 1928, but by that very fact established that fraction not to state the ratio of August, 1927.

In the petition for certiorari, the Government contended that the fact that the four operating companies were grouped under one management made the stock of the holding company more valuable than the aggregate of the four operating companies, but this, as pointed out in our brief in opposition to certiorari, was exactly contrary to the evidence, and the point appears to have been abandoned in the Government's brief on the merits.

The determination of the Commissioner of Internal Revenue in this case was entitled to no presumption of correctness, because it was wrong on its face. The exercise by the Commissioner of his discretion is entitled to weight; but where the Commissioner makes a groundless, capricious, or arbitrary determination, or one erroneous on its face, such determination is not the exercise of the Commissioner's discretion, but a failure to exercise it. Such a determination is not entitled to any presumption of correctness, nor to any *prima facie* weight. It is a mere contradiction in terms to say that a determination wrong on its face is presumptively correct. No court would grant a judgment by default if

the complaint stated no cause of action; yet, even assuming (contrary to the fact) that there was a default, that is precisely analogous to what the Board did here.

The decision of the Board in this case was not supported by any evidence, nor by any presumption. It was directly contrary to competent, uncontradicted evidence, the sufficiency of which was not questioned. The Board made the same error of law made by the Commissioner: its conclusion did not follow as a matter of law from its premise.

II.

The taxpayer introduced substantial evidence tending to prove no additional tax to be due; and, the Board not having decided such evidence to be insufficient, it cannot be said that the taxpayer failed to prove his correct tax liability.

The Government makes no serious contention that the taxpayer failed to sustain the burden of proving the determination of the Commissioner to be wrong. It rests its case upon the proposition that no matter how wrong the Commissioner's determination was, and no matter how wrong the Board was in redetermining the determination of the Commissioner, still it cannot be said that the Board erred as a matter of law, so long as the taxpayer failed to prove at the trial precisely what his correct tax liability was, in addition to proving that it was less than the amount determined by the Commissioner.

While, as we will hereinafter urge, the Government has not shown the requirement of the law to go as far,

nevertheless that question is not raised in this case. The taxpayer unquestionably proved the determination of the Commissioner to be wrong, and he introduced substantial evidence tending to show that he owed no additional tax.

This is not a case of failure of proof of correct tax liability, as contended by the Government. Although, pursuant to the agreed theory of the case, the taxpayer refrained from introducing all of the evidence he might otherwise have introduced, and although the evidence which was introduced was, as pointed out in the Government's brief, addressed to the issue which (as we contend the record establishes) had been stipulated to be the only issue, nevertheless that evidence also tended to show that it was impracticable to make any allocation between the preferred and all the stock of the holding company as of the time of the issuance of that stock. If sufficient, that evidence would have satisfied such burden of proof of his correct tax liability as the taxpayer may have had, for it would have established no tax to be due. The Board was the sole judge of the sufficiency of such evidence,[4] but, by reason of the error of its decision that the Commissioner's allocation was correct, the Board did not decide whether or not the evidence established that no fair allocation was practicable.

The Board decided the Commissioner's allocation to be correct. While it did not in terms hold any fair allocation to be practicable, it may be said to have held, by implication, that the Commissioner's allocation was both fair and practicable, and, by further implication, that the taxpayer's evidence of impracticability was insufficient. But the Board decided by implication only

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4. *Phillips* v. *Commissioner*, 283 U. S. 589, 600.

what was necessary to its decision, and the decision that the Commissioner's allocation was correct was based upon an error of law. The implications of that erroneous decision, therefore, partake of equal error. The Board did not decide that any allocation other than that made by the Commissioner was either fair or practicable, and therefore did not hold, except erroneously in law, that the taxpayer's evidence of impracticability was not sufficient.

Lucas v. *Ox Fibre Brush Co.*, 281 U. S. 115, affirming 32 F. (2d) 42 (C. C. A. 4).

The Board not having held the taxpayer's evidence of impracticability not to be sufficient, it cannot be said that the taxpayer has failed to meet whatever burden he may have had of proving his correct tax liability.

The Court below, it is true, did state in its opinion that, "If the burden of proof goes so far as to demand not only that the taxpayer show that the deficiency assessed against him is wrong, but what is the proper deficiency, or that there should be none at all, the decision was right, even though we know that the tax is too high." This dictum of the Circuit Court of Appeals, taken in its context, which is a discussion of some of the evidence tending to prove impracticability of allocation, does not mean that the Court thought that there was no substantial evidence of impracticability introduced before the Board; it simply indicates a refusal on the part of the Circuit Court to say that the evidence introduced was of such weight as to allow the Court to reverse without remanding, on the ground that the Board could not have failed to find that no allocation was practicable.

The fact is that this is not a case of failure of proof; but a case where, by reason of a mistake of law, the Board disregarded competent evidence.

The whole record in this case tends to show that no apportionment was practicable. The taxpayer owned all of the stock at the outset, and he held the preferred throughout the period in question. Nothing appears in the record to rebut the presumption that he continued to hold all of the common, and, therefore, it appears from the record that there were no sales to evidence respective values for the different classes of stock.

Moreover, the record contains unqualified and uncontradicted testimony that during the time from August, 1927, to May, 1928, the operating companies declared no distributions or dividends (R. 31).[5]

The Board's error of law in disregarding this evidence cannot be questioned, for it stated in its opinion (R. 9) that there was no testimony as to this fact.

While the taxpayer, if it had not been for the stipulation of counsel agreeing to the erroneous theory of the case, might well have introduced cumulative evidence in this regard, at least it cannot be said that the record contains no substantial evidence that it was impracticable to apportion. Surely the Government does not intend to urge that the erroneous theory upon which the case was tried is any reason why the evidence introduced should not be given its full weight and meaning.

The taxpayer contends in this connection that an inference should be drawn from the determination of the Commissioner. The objection of the Circuit Court of Appeals to the finality of the taxpayer's evidence of impracticability was that the financial histories of the operating companies had not been shown. The Com-

5. The record shows (R. 31) that the earnings of the operating companies were between nine and ten thousand dollars a year, though whether this was gross or net did not appear. However, the evidence does indicate that the holding company had substantial expenses, for it employed a firm of supervising engineers (R. 29).

missioner, in making his determination, however, had all of the facts which the taxpayer could have had, for he must have had the income tax returns of the operating companies, and must be presumed to have satisfied himself as to their correctness by audit or otherwise. The Commissioner had fully audited the taxpayer's return and examined his books and records. He had sent the taxpayer two audit letters, proposing additional tax, and had received the taxpayer's statements in protest thereto. The Commissioner was in possession of all of the facts; he must be presumed to have taken the most reasonable action which could be taken in the premises, for such was his duty. When the Commissioner, making the most reasonable allocation which the facts allowed, made an allocation without any foundation in fact and which was absolutely wrong on its face as a matter of law, it would appear proper to infer that no fair allocation could be made.

The Board of Tax Appeals held that the Commissioner's determination should be approved for the reason that the taxpayer had not shown any other allocation, thus assuming (without the support of any evidence or presumption) that some fair allocation was practicable. Had the Board properly applied the law, its decision (passing, for the moment, the fact that the Commissioner's allocation was a mere nullity) would have been that the allocation made by the Commissioner was not a proper allocation, and the Board should then have decided whether any allocation was practicable. But it merely decided that the Commissioner's allocation was practicable, and this being erroneous, the Board has not decided the fundamental question, although evidence tending to show no allocation to be practicable was in fact introduced. The whole thesis of the Government's case is based upon a

failure of proof, but it is submitted that so long as the record contains evidence tending to show both that the Commissioner's determination was wrong and the correct tax liability, and the only decision of the Board has been the erroneous one that the Commissioner's allocation was correct, the foundation for the Government's case does not exist. It cannot be said that there has been any failure of proof, even though it be held that the taxpayer should have proven the correct amount of tax, as well as that the Commissioner's determination was wrong.

III.

Even if the taxpayer's evidence that no additional tax was due were insufficient, still the Board should not have approved the Commissioner's plainly erroneous determination, but should have decided no additional tax to be due, or, in any event, have received the taxpayer's further evidence.

The question argued by the Government, *i. e.*, whether the Board errs in law when it decides that because a taxpayer does not prove his correct tax liability he owes the tax asserted against him by the Commissioner, no matter how conclusively he has proven that he does not, is not presented in this case, because the taxpayer did not fail of his proof. But even if he had failed to prove he owed no additional tax, still that question does not appear.

As we have urged above, the determination of the Commissioner was wrong on its face. Being wrong on its face, it was entitled to no presumption of correctness. And being entitled to no presumption of correct-

ness, it could have raised no burden of proof upon the taxpayer.

When the Commissioner, in the exercise of his discretion, makes a determination, that determination is entitled to a presumption of correctness. Thus the need of the Government expeditiously to collect its revenues is served, but we know of no case suggesting such consequences to flow from a determination of the Commissioner based upon his failure or refusal to exercise his discretion.

Whether or not the Commissioner acting on some reasonable ground may, by a denial of the correctness of an item on the return of a taxpayer, force the taxpayer to come forward and prove that the item was correct not only in respect of the Commissioner's question, but also in all other respects, surely the mere caprice of the Commissioner can place no such burden on the taxpayer.

Like the decision of the Board, the only determination of the Commissioner that any fair allocation was practicable is one implied by his determination that the allocation he determined ought to be made. Inasmuch as that determination was wrong as a matter of law, it cannot be said that there has been any determination that any fair allocation was practicable.

The purported determination of the Commissioner having been merely arbitrary in this case, the correctness of the taxpayer's return has not been questioned and ought to be affirmed.

The Board of Tax Appeals has held that where the Commissioner's determination is wrong upon its face, it is a nullity; and that a decision approving the return should be entered.

Appeal of Bruce & Human Drug Co., 1 B. T. A. 342;

Appeal of Index Notion Co., 3 B. T. A. 90.

In both of these decisions, the Commissioner has formally acquiesced.[6]

But even if the Commissioner's determination were not arbitrary, still the fact that the case was tried by all upon a mistaken theory of law is an irregularity which should be corrected by reversing the decision of the Board and remanding for a new trial.

The Government admits in its brief that the case was indeed tried, by the taxpayer, exclusively upon the theory referred to, but states that the Commissioner denied that he had agreed thereto. This statment, however, appears to be based upon a misapprehension of fact.[7] The record contains two affidavits of reputable persons, one of whom was the taxpayer's attorney before the Board, and the other of whom, the taxpayer's accountant, was also present at the trial, stating, on knowledge, that such agreement took place. These affidavits stand uncontradicted on the record.

The only foundation for the statement, of which we are aware, is that in its brief in the Circuit Court of Appeals the Government did state that such agreement was "not admitted." Inasmuch as that statement does not appear upon the record, we ask leave to add that at the hearing before the Board on the taxpayer's motion for new trial, the Commissioner's counsel, who had conducted the trial, stated that he did not remember whether or not he had made such agreement.

It is submitted that the record establishes such agreement to have been made.

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6. C. B. IV-1, p. 1;
C. B. V-2, p. 2.
7. This error was promptly called to the attention of the Government by letter dated November 21, 1934, to which reply was made that explanation or correction would be made in oral argument.

As stated in the affidavits of William P. Jeffery and Walter R. Bullock (R. 17, 18), the case was tried upon the theory, agreed to by the Commissioner, and tacitly approved by the presiding Member of the Board, that if it were shown that the value of the stocks of the operating companies, at the time the same were acquired by the holding company, did not exceed their cost to the taxpayer, then there was no additional tax.

This, it is submitted, amounts to prejudicial error which can be corrected only by a rehearing, for, had it not been for such agreement, the taxpayer might well have introduced at the trial the further evidence offered in his motion for new trial.

In *Wyoming Investment Co.* v. *Commissioner*, 70 F. (2d) 191 (C. C. A. 10), the facts as to trial upon an agreed but erroneous theory were almost identical with the facts in the instant case, and the Circuit Court of Appeals reversed and remanded. In that case, the Government states, no review was sought.

Even where there has been no agreement, but, through some misfortune or misunderstanding, or due to trial on an erroneous theory, the taxpayer has failed to prove his correct tax liability, the Circuit Courts have reversed and remanded; and this rule would appear to be particularly applicable where, as here, the Commissioner's determination was positively wrong and further evidence is available.

Underwood v. *Commissioner*, 56 F. (2d) 67 (C. C. A. 4);

Virginia-Lincoln Furniture Corp. v. *Commissioner*, 56 F. (2d) 1028 (C. C. A. 4);

Ferguson v. *Commissioner*, 59 F. (2d) 893 (C. C. A. 10);

Commissioner v. *Wright*, 47 F. (2d) 871 (C. C. A. 7).

And such has always been the duty of appellate courts.

> *Bright* v. *Eynon,* 1 Burr. 390, 395; 97 Reprint 365;
> *Dermott* v. *Wallach,* 66 U. S. (1 Black) 96, 98;
> *American Products Co.* v. *Refining Co.,* 275 Pa. 332, 337.

While we believe it to be clear that the question of the extent of the taxpayer's burden of proof does not arise in this case, we point out that no case cited by the Government goes so far as to hold that where, in a proceeding before the Board of Tax Appeals, the determination of the Commissioner has been established to be absolutely wrong, the Board may, nevertheless, decide it to be correct.

As pointed out in our brief in opposition to certiorari, while in some cases the Courts have indeed used language indicative of such a duty, the fact in each of the cases cited in the petition for the proposition that the taxpayer before the Board must prove the correct amount of tax, was that the taxpayer had not proven the Commissioner to be wrong. As we there suggested, the reason for the existence of such language appears to be that the most feasible disproof of one fact is, oftentimes, proof of a contrary fact. As illustrative of that point, we quoted from that part of the opinion in *Darcy, et al.* v. *Commissioner* (C. C. A. 2), 66 F. (2d) 581, 585, certiorari denied 290 U. S. 705, which was quoted in the petition (and repeated in the Government's brief on the merits), as follows:

> "The burden is upon the petitioners to show the correct amount of the tax *in order to show that the Commissioner's determination was wrong.* * * *"
> (Italics supplied).

As further evidence of that fact, we pointed out that *Matern* v. *Commissioner* (C. C. A. 9), 61 F. (2d) 663, cited by the Government in the petition (and its brief on the merits) for the same proposition, has been cited in a later case by the same Court for the proposition that:

> "* * * This court has held that 'the presumption of correctness is attached to the Commissioner's findings'. *Matern* v. *Comm'r.*, 61 F. (2d) 663, 666. So from the outset the determination by the Commissioner of the fair market value of the property in question was *prima facie* correct and the burden of establishing it as incorrect was upon the petitioner."
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> *Old Mission Portland Cement Co.* v. *Commissioner* (C. C. A. 9), 69 F. (2d) 676, 679; certiorari granted Oct. 8, 1934, (55 S. Ct. 79) not officially reported.

In its brief on the merits the Government cites the same and other cases, but we submit that neither any case cited before, nor any cited for the first time in the brief on the merits, stands for any more than that the Board will be affirmed in approving the determination of the Commissioner, where the taxpayer has failed to prove that determination to be wrong.

On the contrary, as we pointed out in our brief in opposition, the Circuit Courts of Appeals for every Circuit and the Court of Appeals of the District of Columbia have held that where the determination of the Commissioner has been proven to be wrong, the Board may not approve the erroneous determination of the Commissioner on the ground that evidence sufficient to form the basis for a decision on the merits has not

been introduced.[8] In the Third Circuit, the rule has been laid down that where the determination of the Commissioner has been shown to be wrong, the Commissioner must show why the return should not be approved.[9]

Pittsburgh Hotels Co. v. *Commissioner, supra,* footnote 8;
Nichols v. *Commissioner, supra,* footnote 8.

In the other Circuits such cases are sent back for further facts, unless the evidence is sufficient to permit the Court to make a decision on the merits. See cases cited *supra,* footnote 8.

We have found no discussion of this question in any decision of this Court, except that, in his dissenting opinion in *Freuler* v. *Helvering,* 291 U. S. 35, in which Mr. Justice Brandeis and Mr. Justice Stone concurred, Mr. Justice Cardozo stated that by the decision in that case the taxpayer was relieved of proving the amount of the Commissioner's error; and said, at p. 51:

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8. *Rhode Island Hospital Trust Co.* v. *Commissioner* (C. C. A. 1) 29 F. (2d) 339;
Conrad & Co., Inc. v. *Commissioner* (C. C. A. 1) 50 F. (2d) 576;
Cohan v. *Commissioner* (C. C. A. 2) 39 F. (2d) 540;
Pittsburgh Hotels Co. v. *Commissioner* (C. C. A. 3) 43 F. (2d) 345;
Nichols v. *Commissioner* (C. C. A. 3) 44 F. (2d) 157;
Strother v. *Commissioner* (C. C. A. 4) 55 F. (2d) 626, aff'd 287 U. S. 308;
Underwood v. *Commissioner* (C. C. A. 4) *supra;*
Independent Ice & Cold Storage Co. v. *Commissioner* (C. C. A. 5) 50 F. (2d) 31;
Collin v. *Commissioner* (C. C. A. 6) *supra;*
Eau Claire Book & Stationery Co v. *Commissioner* (C. C. A. 7) 65 F. (2d) 125;
Kendrick Coal & Dock Co. v. *Commissioner* (C. C. A. 8) 29 F. (2d) 559;
Citrus Soap Co. of California v. *Lucas* (C. C. A. 9) 42 F. (2d) 372;
Ferguson v. *Commissioner* (C. C. A. 10) *supra;*
Kirkland v. *Burnet* (App., D. C.) *supra;*
Dempster Mill Mfg. Co. v. *Burnet* (App., D. C.) 46 F. (2d) 604.

9. The burden of proof as to deficiencies not asserted in the original notice is on the Commissioner. B. T. A. Rules of Practice, Rule 30, *infra,* p. 30

> "* * * The Commissioner's assessment is supported by a presumption of correctness. If a taxpayer would overthrow it, he has the burden of proving it erroneous, and of fixing in dollars and cents the amount of the error. By the decision just announced, the taxpayer is relieved of that burden. * * *"

As we contend, the Board may not, without committing error, decide that a taxpayer owes a tax which he has proven he does not owe, at least where there is ground to believe that at another trial evidence, not theretofore introduced by reason of some mistake or misfortune, may be available in order to establish the true tax liability.

We submit that the distinction made by the Court below as respects the difference between suits for refund and proceedings before the Board of Tax Appeals concerning asserted deficiencies in tax, is correct. In a suit for refund, a taxpayer is asking a money judgment against the United States (or the Collector), and it is fundamental that to obtain such a judgment he must show every dollar that is due him.

In *Becker* v. *United States*, 21 F. (2d) 1003 (C. C. A. 5), as pointed out in our brief in opposition to certiorari, the taxpayer had reported its income upon a basis which, it was found, did not correctly reflect income. The Commissioner made an assessment on a basis, which, although not exact, was "as nearly accurate as it was possible to make from the company's books". In the *Becker* case, it did appear that the Commissioner's determination was erroneous to some extent, and the Court did, nevertheless, uphold it. It was so upheld, however, upon the basis that the Commissioner's determination was "as nearly accurate as it was possible to make from the company's books". As

contended in our brief in opposition to certiorari, the case presents a special situation, and the same Court subsequently decided *Independent Ice & Cold Storage Company* v. *Commissioner, supra,* without reference to it. In any event, the *Becker* case did not involve a proceeding before the Board, but before a court.

In *United States* v. *Rindskopf, et al.,* 105 U. S. 418, this Court, speaking through Mr. Justice Field, stated that, to the extent to which an assessment is not impaired by the evidence, it remains due. That case was a suit upon a distiller's bond founded upon an alleged tax due. It appeared that the defendant therein did establish that the entire amount of the assessment was not due, but did not establish that some part thereof was not due. It is significant to note that in the *Rindskopf* case this Court remanded for a new trial, as was done by the Court below in the instant case.

Conclusion.

In conclusion, it is respectfully submitted that where a taxpayer has proven that he does not owe the tax asserted against him, but the Board holds that sufficient evidence has not been introduced to serve as a basis for a decision on the merits, and approves the erroneous determination of the Commissioner, a Circuit Court of Appeals properly reverses the erroneous decision of the Board and remands the case for the taking of further evidence, at least where it appears that such evidence is available.

That question, however, is not raised in this case. The determination of the Commissioner was wrong on its face, and was a mere nullity which did not operate to question the taxpayer's return. Moreover, the case was tried under such circumstances that the decision of

the Board, without receiving the taxpayer's further evidence, was an irregularity which should be corrected by a rehearing.

And in any event, as we contend, the taxpayer did not fail in his proof either as to proving the Commissioner's determination to be wrong, or as to proving that he owed no additional tax.

The decision of the Board was erroneous in law. From the evidence in the record, the conclusion appears to be irresistible that the taxpayer did not owe an additional tax in any such amount as has been collected from him, or, indeed, in any amount. In any event, further and cumulative evidence in this regard is available and has been offered. It is submitted that the decision of the Court below was appropriate and just and correct in law; and ought to be affirmed.

Dated: New York, N. Y., November 28, 1934.

Respectfully submitted,

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APPENDIX.

Revenue Act of 1926, c. 27, 44 Stat. 9, 110:

SEC. 1003. (a) The Circuit Courts of Appeals and the Court of Appeals of the District of Columbia shall have exclusive jurisdiction to review the decisions of the Board (except as provided in section 239 of the Judicial Code, as amended); and the judgment of any such court shall be final, except that it shall be subject to review by the Supreme Court of the United States upon certiorari, in the manner provided in section 240 of the Judicial Code, as amended.

(b) Upon such review, such courts shall have power to affirm or, if the decision of the Board is not in accordance with law, to modify or to reverse the decision of the Board, with or without remanding the case for a rehearing, as justice may require. (U. S. C. App., Title 26, Sec. 1226.)

Revenue Act of 1928, c. 852, 45 Stat. 791, 815, 818:

SEC. 111. DETERMINATION OF AMOUNT OF GAIN OR LOSS.

(a) *Computation of gain or loss.*—Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the basis provided in section 113, and the loss shall be the excess of such basis over the amount realized.

* * * * *

(d) *Recognition of gain or loss.*—In the case of a sale or exchange, the extent to which the gain or loss determined under this section shall be recognized for the purposes of this title, shall be determined under the provisions of section 112. * * *

SEC. 113. BASIS FOR DETERMINING GAIN OR LOSS.

(a) *Property acquired after February 28, 1913.*—The basis for determining the gain or loss from the sale or other disposition of property acquired after February 28, 1913, shall be the cost of such property: except that—

* * * * *

(6) *Tax-free exchanges generally.*—If the property was acquired upon an exchange described in section 112 (b) to (e), inclusive, the basis shall be the same as in the case of the property exchanged, decreased in the amount of any money received by the taxpayer and increased in the amount of gain or decreased in the amount of loss to the taxpayer that was recognized upon such exchange under the law applicable to the year in which the exchange was made. * * *

Treasury Regulations 74:

ART. 58. *Sale of stock and rights.* * * * Where common stock is received as a bonus with the purchase of preferred stock or bonds, the total purchase price shall be fairly apportioned between such common stock and the securities purchased for the purpose of determining the portion of the cost attributable to each class of stock or securities, but if that should be impracticable in any case, no profit on any subsequent sale of any part of the stock or securities will be realized until out of the proceeds of sales shall have been recovered the total cost. * * *

Rules of Practice Before The United States Board of Tax Appeals:

Rule 30.—*Burden of Proof.* The burden of proof shall be upon the petitioner, except as otherwise provided by statute and except that in respect of any new matter pleaded in his answer, it shall be upon the respondent.

SUPREME COURT OF THE UNITED STATES.

No. 289.—October Term, 1934.

Guy T. Helvering, Commissioner of Internal Revenue, Petitioner, *vs.* Walter W. Taylor.	On Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit.

[January 7, 1935.]

Mr. Justice Butler delivered the opinion of the Court.

The commissioner determined a deficiency of $9,156.69 on account of respondent's 1928 income tax. The Board of Tax Appeals made the same determination. The court held it excessive and that the evidence did not show the correct amount, reversed the order of the board and remanded the case for further proceedings in accordance with the opinion. 70 F. (2d) 619. The petition for our writ states the question: "Whether the Circuit Court of Appeals erred in remanding this case to the Board of Tax Appeals for a new hearing on the ground that the Commissioner's determination of the amount of income was incorrect, although the taxpayer had failed to prove facts from which a correct determination could be made".

In August, 1927, respondent acquired all the stock of four utilities at a total cost of $96,030, organized a holding company and October 13 transferred to it all the utilities stock and received therefor all the shares of the holding company: 1,000 of preferred having no par value, entitled to a dividend of $6 annually, $100 on liquidation and callable at $105 per share; 2,500 of no par value class A common callable at $35 per share; 5,000 of no par value class B common stock having the voting power. As this transaction was "reorganization" under Revenue Act of 1926, § 203 (b) (2), 44 Stat. 12, no taxable gain resulted.

In May, 1928, the holding company sold the stock of the four utilities to the Colonial corporation for $194,930.16. Later in that year the holding company bought or retired all the preferred and paid the taxpayer $99,000 therefor. In his 1928 return he assigned

the $96,030 for which he procured the utilities to the preferred stock of the holding company; deducted that amount from the $99,000 received therefor, and reported the difference, $2,970, as the gain derived from the sale. The applicable statutory provisions are contained in Revenue Act of 1928, §§ 111 (a) (d), 112 (b) (3), 113 (a) (6). 45 Stat. 815-19.[1] They prescribe no rule that is applicable for the ascertainment of the cost of the preferred stock or the apportionment of the total cost between preferred and common. But Regulations 74, Art. 58, declares: "Where common stock is received as a bonus with the purchase of preferred stock or bonds, the total purchase price shall be fairly apportioned between such common stock and the securities purchased for the purpose of determining the portion of the cost attributable to each class of stock or securities, but if that should be impracticable in any case, no profit on any subsequent sale of any part of the stock or securities will be realized until out of the proceeds of sales shall have been recovered the total cost".

The Commissioner, holding the taxpayer not entitled to charge the cost of all to the preferred, apportioned between the preferred and common. He made his calculation upon the assumption that the cost, in 1927, attributable to the preferred shares bears the same relation to cost of all the shares then acquired as the amount

[1] "Sec. 111. (a) Except as hereinafter provided in this section, the gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the basis provided in section 113, and the loss shall be the excess of such basis over the amount realized. . . .

"(d) In the case of a sale or exchange, the extent to which the gain or loss determined under this section shall be recognized for the purposes of this title, shall be determined under the provisions of section 112.

"Sec. 112. (b) (3) No gain or loss shall be recognized if stock or securities in a corporation a party to a reorganization are, in pursuance to the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization.

"Sec. 113. (a) The basis for determining the gain or loss from the sale or other disposition of property acquired after February 28, 1913, shall be the cost of such property; except that . . .

"(6) If the property was acquired upon an exchange described in section 112 (b) to (e), inclusive, the basis shall be the same as in the case of the property exchanged, decreased in the amount of any money received by the taxpayer and increased in the amount of gain or decreased in the amount of loss to the taxpayer that was recognized upon such exchange under the law applicable to the year in which the exchange was made." 45 Stat. 815-819.

respondent received, in 1928, for the preferred bears to the amount paid the holding company by Colonial corporation for all the utilities shares.[2] On that basis, he found that of the total 1927 cost, $96,030, there was chargeable to the preferred only $48,771.16 which deducted from $99,000 received by respondent for the preferred in 1928, leaves $50,228.84 upon which he determined the deficiency of $9,156.69.

Before the Board of Tax Appeals the taxpayer introduced evidence to show the details of the transaction and that there was no change in value of the utilities stock between the time he got it in August, 1927, and the date, October 13 of the same year, on which he transferred it to the holding company in exchange for its shares and that the entire increase in value came after that transfer. No opposing evidence was offered. On the facts shown, the taxpayer maintained that, as total cost was less than $100 per share for the preferred having prior rights to that extent on liquidation, the common stock had no value. Rejecting that contention, the Board of Tax Appeals filed a memorandum opinion in which it said: "It may well be that the properties acquired or all the classes of stocks received by the petitioner were worth only $96,030 . . . and yet the preferred stock . . . may have had the value of $48,771.16 . . . It is obvious that even if all the securities were worth only $96,030 that the proportionate value of the preferred stock to all the stocks would not necessarily be different from that determined by the Commissioner. . . . The question . . . is one of fact to be determined by testimony and not theory. It is conceivable that common stocks may actually sell on the market when preferred stocks in the same corporation are selling at less than par". It was upon that basis, without specific findings of fact, that the board made the redetermination at the figure set by the commissioner.

The only question for consideration is that stated in the petition for the writ of certiorari. *Gunning* v. *Cooley*, 281 U. S. 90, 98. That question in effect assumes, and here it is taken as granted, that the court rightly held the evidence sufficient to re-

[2]The figures are: X : $96,030 : : $99,000 : $194,930.17. The calculation stated in the opinion of the Board of Tax Appeals is:

$$\frac{\$99,000.00}{\$194,930.17} \times \$96,030 = \$48,771.16.$$

quire a finding that the commissioner's apportionment of total cost as between preferred and common stock was unfair and erroneous and that therefore the commissioner's determination was excessive. We also assume that the total purchase price is susceptible of fair apportionment and that upon another hearing the correct amount may be found. 70 F. (2d) 619, 620. Regulations 74, Art. 58, *supra*. The point to be considered is whether, the taxpayer having failed to establish the correct amount to be assigned to the preferred stock as its cost to him, the court erred in reversing and remanding for further proceedings in accordance with its opinion.

The commissioner does not contend that, in cases where Circuit Courts of Appeals properly reverse determinations of the board they are without power to remand for further hearing in the nature of a new trial.[3] His contention is that in this case the burden on the taxpayer was not only to prove that the commissioner's determination is erroneous but to show the correct amount of the tax. In substance he says that, because of the taxpayer's failure to establish facts on which a fair apportionment may be made, the board's redetermination at the commissioner's erroneous figure was valid and there being no error of law should have been sustained by the court. And he maintains that, in the absence of error on the part of the board, the court was without power to remand for further hearing.

He cites Revenue Act of 1926, § 274 (e) 44 Stat. 56: "The Board shall have jurisdiction to redetermine the correct amount of the deficiency even if the amount so redetermined is greater than the amount of the deficiency, notice of which has been mailed to the taxpayer, and to determine whether any penalty, additional amount or addition to the tax should be assessed, if claim therefor is asserted by the Commissioner at or before the hearing or a rehearing". The purpose of that provision is to define the jurisdiction granted to the board; it does not prescribe any rule of evidence or burden of proof. Plainly it does not support the commissioner's contention that the taxpayer, even though he has shown

[3] § 1003 (b), Revenue Act of 1926, 44 Stat. 110, 26 U. S. C. Sup. VII, § 641 (c) (1) provides: "Upon such review, such courts shall have power to affirm or, if the decision of the Board is not in accordance with law, to modify or to reverse the decision of the Board, with or without remanding the case for a rehearing, as justice may require".

the determination to be arbitrary and excessive, must nevertheless pay the added tax because he has not also shown that he owes nothing or the correct amount, if any, that legally may be laid upon him.

He also cites Revenue Act of 1928, §§ 51 (a) and 54 (a). 45 Stat. 807, 808. Neither gives any support to his contention. The first requires the taxpayer to make under oath a return stating specifically the amount of his gross income and the amounts of deductions and credits allowed. The other requires the taxpayer to keep such records, render under oath such statements, make such returns, and comply with such rules and regulations as the commissioner may prescribe. These requirements give no support to the commissioner's contention. They tend rather to suggest that taxpayers' returns are correct and may not arbitrarily be set at naught.

He also cites Rule 30 adopted by the board: "The burden of proof shall be upon the petitioner, except as otherwise provided by statute and except that in respect of any new matter pleaded in his answer, it shall be upon the respondent". But there is nothing in it to suggest intention to require the taxpayer to prove not only that a deficiency assessment laid upon him was arbitrary and wrong but also to show the correct amount. Moreover, the board held the evidence not sufficient to show the apportionment erroneous and on that ground alone sustained the assessment. Necessarily the board did not come to the question that is here presented as to burden of proof. The fact that the commissioner's determination of a deficiency was arbitrarily made may reasonably be deemed sufficient to require the board to set it aside. Cf. *Bruce & Human Drug Co.*, 1 B. T. A. 342. *Acorn Refining Co.*, 2 B. T. A. 253. *Index Notion Co.*, 3 B. T. A. 90.

The commissioner cites *United States* v. *Rindskopf*, 105 U. S. 418; *United States* v. *Anderson*, 269 U. S. 422, 443; *Reinecke* v. *Spalding*, 280 U. S. 227, 232-233. The first of these may be put aside without discussion as having no bearing upon the point here in controversy. The other two were adequately distinguished by the Circuit Court of Appeals. Each was an action to recover taxes paid. Obviously the burden was on the plaintiff, in order to establish a basis for judgment in his favor, specifically to show not merely that the assessment was erroneous but also the amount to which he was entitled. For like reason the burden is upon the

taxpayer to establish the amount of a deduction claimed. *Burnet* v. *Houston*, 283 U. S. 223, 227. *Helvering* v. *Ind. Life Ins. Co.*, 292 U. S. 371, 381. *New Colonial Co.* v. *Helvering*, 292 U. S. 435, 440.

We find nothing in the statutes, the rules of the board or our decisions that gives any support to the idea that the commissioner's determination shown to be without rational foundation and excessive will be enforced unless the taxpayer proves he owes nothing or, if liable at all, shows the correct amount. While decisions of the lower courts may not be harmonious, our attention has not been called to any that persuasively supports the rule for which the commissioner here contends.[4]

Unquestionably the burden of proof is on the taxpayer to show that the commissioner's determination is invalid. *Lucas* v. *Structural Steel Co.*, 281 U. S. 264, 271. *Wickwire* v. *Reinecke*, 275 U. S. 101, 105. *Welch* v. *Helvering*, 290 U. S. 111, 115. Frequently, if not quite generally, evidence adequate to overthrow the commissioner's finding is also sufficient to show the correct amount, if any, that is due. See, e. g., *Darcy* v. *Commissioner*, 66 F. (2d) 581, 585. But, where as in this case the taxpayer's evidence shows the commissioner's determination to be arbitrary and excessive it may not reasonably be held that he is bound to pay a tax that confessedly he does not owe, unless his evidence was sufficient also to establish the correct amount that lawfully might be charged against him. On the facts shown by the taxpayer in this case, the board should have held the apportionment arbitrary and the commissioner's determination invalid. Then, upon appropriate application that further hearing be had, it should have heard

[4]The Commissioner cites: Hubinger *v.* Commissioner, 36 F. (2d) 724. Sanderson *v.* Commissioner, 42 F. (2d) 160. Autosales Corp. *v.* Commissioner, 43 F. (2d) 931. Onondaga Co. *v.* Commissioner, 50 F. (2d) 397. Darcy *v.* Commissioner, 66 F. (2d) 581, 585. Saxman Coal & Coke Co. *v.* Commissioner, 43 F. (2d) 556. Williams *v.* Commissioner, 45 F. (2d) 61. Alexander Sprunt & Son *v.* Commissioner, 64 F. (2d) 424. Atlantic Bank & Trust Co. *v.* Commissioner, 59 F. (2d) 363. Lightsey *v.* Commissioner, 63 F. (2d) 254. Matern *v.* Commissioner, 61 F. (2d) 663. Atlanta Casket Co. *v.* Rose, 22 F. (2d) 800. Becker *v.* United States, 21 F. (2d) 1003.

Cf. Collin *v.* Commissioner, 32 F. (2d) 753. Citrus Soap Co. of California *v.* Lucas, 42 F. (2d) 372. Russell *v.* Commissioner, 45 F. (2d) 100, 103. Strother *v.* Commissioner, 55 F. (2d) 626, 632. And see, involving deduction, Underwood *v.* Commissioner, 56 F. (2d) 67, 72.

evidence to show whether a fair apportionment might be made and, if so, the correct amount of the tax. The rule for which the commissioner here contends is not consonant with the great remedial purposes of the legislation creating the Board of Tax Appeals.[5] The Circuit Court of Appeals rightly reversed and remanded the case for further proceedings in accordance with its opinion.

Affirmed.

A true copy.

Test:

Clerk, Supreme Court, U. S.

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[5]House Report No. 179, p. 7; Senate Report No. 398, pp. 8-9, 68th Congress, 1st Session. Warren Mfg. Co. *v.* Tait, 60 F. (2d) 982, 984. Old Colony Tr. Co. *v.* Comm'r Int. Rev., 279 U. S. 716, 721.

Mr. Justice STONE.

I think the judgment should be reversed.

As respondent failed to establish any amount by which the deficiency fixed by the Commissioner should be reduced, the Board of Tax Appeals was without authority, under the statute defining its jurisdiction, to disturb the determination of the Commissioner, c. 27, §§ 274 (b) (e), 906 (c) (d), 44 Stat. 9, 55, 56, 107; 26 U. S. C., §§ 1048a, 1048c, 1217 (c) (d). If, under § 906 (d), it was the duty of the Board to dismiss the petition and enter on its records a finding that it could not determine the amount of the deficiency, these requirements are formal only. Its failure to comply with them does not require a reversal of its order sustaining the action of the Commissioner or in any case afford ground for decision on appeal that the Board should have held the Commissioner's determination invalid or that it should now take further evidence.